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IN THE

Supreme Court of the United States.

OCTOBER TERM, No. 413.

FRANK W. MERRICK, JOHN W. HAARER and GRANT FELLOWS,
Appellants,

against

N. W. HALSEY & COMPANY *et al.*, and the WEIS FIBRE CONTAINER CORPORATION,
Appellees.

BRIEF FOR APPELLEES OTHER THAN THE WEIS FIBRE CONTAINER CORPORATION ET AL.

Statement.

The statement by the appellants should be supplemented as follows:

The intervenors Remick, Hodges & Company, a partnership, have no place of business in Michigan and are not sending any agents into the state, but are endeavoring to secure business in said State, and sell securities therein as a part of their general business carried on in the City of New York, by agents and by mail throughout the United States: The volume of their business in Michigan and the value thereof is not sufficient to enable them or

justify them in attempting to comply with the act, and the act if enforced against them would have the effect of preventing them from making any offerings in said State, from establishing any business therein, and from selling securities therein. The act entirely prevents them from developing and extending their business in the State of Michigan (Supplemental Record, pp. 3 and 4).

The Attorney General is in error in the statement made on page 73 of his brief that there is no allegation that the "intervenors do not maintain offices and places of business within the State."

The objections to the act upon which these appellees rely are

First: That it violates the XIVth Amendment of the Federal Constitution.

Second: That it violates Section 8 of Article I of the Federal Constitution by imposing a burden upon Interstate Commerce.

The Michigan Act.

The statute of Michigan which is the basis of the complaint in this suit, was approved by the Governor April 9th, 1915, Act No. 46 (Rec. pp. 63-75).

Section 1 creates a Commission.

Section 2 designates every person, incorporated or unincorporated, who by himslf, itself or others, sells or negotiates for the sale of stocks, bonds or other securities, issued by him or them within the State of Michigan, as an *"investment company."* If a resident of, or organized in, the State of Michigan, as a *domestic* investment company; otherwise, as a *foreign* investment company.

Section 3 exempts from the provisions of the act eight classes of securities, one of which is "securi-

ties which are listed in any standard manual of information approved by said Commission," but the Commission is empowered by special order to suspend the sale of any such listed securities upon its finding that the sale would work a fraud.

Section 10 designates as a *"dealer,"*

> "any person, firm, copartnership, corporation or association whether domestic or foreign, not the issuer, who shall in this State sell or offer for sale any of the stocks, bonds or other securities issued by any foreign or domestic investment company, except the securities specially exempted in this act, or who shall by advertisement or otherwise profess to engage in the business of selling or offering for sale such securities,"

and forbids a dealer to sell or offer for sale any such securities, or profess the business of selling or offering for sale such securities, unless and until he shall have filed a list of the same with the Commission. It excludes from the definition "an owner not issuer, of such securities so owned by him when such sale is not made in the course of continued and successive transactions of a similar nature."

By Section 11, any "dealer" desiring to sell or offer for sale within the State of Michigan any stocks, bonds or other securities not exempted under the terms of the act, must first register with the Michigan Securities Commission, and furnish in such form as it may require, upon oath, the following information: The dealer's name, residence and business address, the general character of the securities to be dealt in, the place or places where the business is to be conducted within this State,

and where the business in this State is not to be conducted by the dealer in person, then the names and addresses of all persons in charge thereof. He must pay a fee of $50, and furnish the Commission with such other information in addition to that above specified as the Commission shall deem necessary in order to thoroughly acquaint it with the character of the dealer's business. All authorized agents of any dealer must be registered with the Commission. No agent shall act as such until so registered. If the dealer be a non-resident of Michigan or a foreign corporation, he shall at the time he registers file with the Commission a written duly authenticated appointment of the Commissioner of the State Banking Department of Michigan as his or its agent in Michigan upon whom process or pleadings may be served for and on behalf of the dealer, "which appointment shall be irrevocable." Upon compliance with these provisions, the Commission must issue to the dealer a license which "shall be good until revoked by said Commission for good cause upon notice to the dealer and a hearing duly had."

Section 14 makes it unlawful for any "investment company" or dealer or representative thereof, directly or indirectly, to sell, cause to be sold, offered for sale, take subscriptions for, or negotiate for sale, in any manner in the State of Michigan, any stocks, bonds or other securities not exempted in the act, unless and *until the Commission has approved* thereof and issued its certificate in accordance with the act. "Nor shall it be lawful for any such investment company to transact business on any other plan than that set forth in the statements and papers required to be filed by virtue

of the provisions of the act or the rules of the Commission." Makes it unlawful for any such company, dealer or agent, to issue, circulate or deliver any advertisement, circular, prospectus, or other document in regard to its stocks, bonds or other securities in the state differing in any way from the copy filed with the Commission. Makes it unlawful for any newspaper published in the State of Michigan to advertise the sale of any stocks, bonds or securities which have not been approved by the Commission or exempted under the provisions of the act.

By Section 15, no "dealer" shall sell, or offer for sale, within the State of Michigan any of the stocks, bonds or other securities of any "investment company" until such company shall have fully complied with the provisions of the act, nor until the "dealer" shall have been registered with the Commission under the terms of the act. Then follows a somewhat ambiguous proviso, reading as follows:

> "Provided, however, that should any dealer desire to sell, or offer for sale, within this State the stocks, bonds or other securities of an investment company which has not itself complied with the provisions of this act, said dealer shall make application to said Commission for license as hereinbefore provided for applications by investment companies, and shall pay the same fee required to be paid by said investment company."

Section 4 provides that before selling, offering for sale, taking subscriptions for, or negotiating for sale in the State of Michigan, any stocks, bonds or other securities of its own issue, every investment company, domestic or foreign, shall file in the office of the Commission a statement showing in full detail, (1) the plan upon which it proposes

to transact business; (2) a copy of all contracts, stocks, bonds or other instruments which it proposes to make with, or sell to, its contributors or customers; (3) a copy of its prospectus and of the proposed advertisement of its sale of stocks, bonds or other securities, showing (4) the name and location and main office of the investment company, the names and addresses of its officers, and an itemized account of its financial condition and the amount of its assets and liabilities, and such other information touching its condition and affairs as the Commission may require. If it be a partnership, it must file a copy of its articles of copartnership or association and all other papers pertaining to its organization; if a corporation, a copy of its articles of incorporation, constitution and by-laws and other papers; if it be organized under the laws of another State, a copy of the laws under which it exists or is incorporated, besides a copy of its charter, etc., and a certificate of the proper officer of such State showing that it is authorized to transact business there, and it must pay a filing fee of not less than $10 nor more than $100.

By Section 6, every foreign investment company before offering for sale any of its stocks, bonds or other securities in Michigan, must file "its irrevocable written consent that suits and actions may be commenced against it in the proper Court of any county in this State in which a cause of action may arise or in which the plaintiff may reside, by the service of any process or pleadings authorized by the laws of this State, on the Commissioner of the State Banking Department."

No formal requirement respecting application for the permission provided for in subsequent sec-

tions is contained in the act, but Section 7 assumes that the application is required, by enacting that "said application shall be heard by the said Commission at the next regular meeting after said application is filed (providing such filing shall precede such monthly meeting by twenty-four hours), or at a special or adjourned meeting of said Commission", at least two days' notice of which shall be given to the applicant.

Section 8, empowers the Commission to demand of any investment company seeking to come under the provisions of the act "any further information other than such investment company is required to furnish under the provisions of this act which shall be necessary to the end that the Commission may be put in possession of all facts and information necessary to qualify it to properly pass upon all questions that may come before it. It may make or have made under its direction a detailed examination of such investment company's property, business and affairs, which examination shall be at the expense of such investment company. It may cause an appraisal to be made, at the expense of said investment company, of the property of said investment company including the value of patents, good will, promotion and intangible assets, and it may fix the amount of stocks, bonds and securities that shall be issued by any corporation, foreign or domestic, in payment for property, patents, good will, promotion and intangible assets at the value it shall find the same to be worth and may require that such stocks and securities so issued for such property, patents, good will, promotion and intangible assets shall be deposited in escrow under such terms as said Commission may prescribe." It may withhold its license to sell stocks, etc., if such

corporation has issued the same for property, patents, good will, promotion and intangible assets "in excess of their value as found by said Commission or if said stocks, bonds and securities are not deposited in escrow according to the terms fixed by such Commission until such stocks, bonds and securities issued in payment for property, patents, good will, promotion and intangible assets in excess of the value so found by said Commission have been surrendered to such corporation and cancelled by it, and until the said stock has been deposited in escrow under the terms prescribed by said Commission."

By Section 9, it is made the duty of the Commission to examine the statements and reports filed with it, and to hear the applicant, and it is given the power to examine under oath any person interested in or connected with the investment company. "And if said Commission finds that the proposed plan of business of said investment company, or that its proposed contracts, stocks, bonds or other securities are fraudulent or *are of such a nature that the sale of such contracts, stocks, bonds or other securities would in the opinion of said Commission work a fraud upon the purchaser,* then said Commission shall disapprove the sale of such proposed contracts, stocks, bonds or other securities and shall notify such investment company by registered mail of its findings and disapproval, and it shall be unlawful for such company to do any business in the way of selling, offering for sale, taking subscriptions for, or negotiating for the sale in any manner whatever of any such contracts, stocks, bonds and other securities in this State; and said contracts, stocks, bonds and other securities shall not be sold in this State." But if the

Commission "shall not find" either of the conclusions last stated, "it shall approve the sale" and issue a certificate in the form prescribed, giving "permission" to sell the same within the State.

Section 13, attempts to regulate the manner in which the accounts of every "investment company," domestic or foreign, shall be kept, and requires their books of account to be open at all times during business hours to stockholders and investors in said company and to the Commission, or its duly authorized representatives, and provides that *all* such investment companies shall be subject to examination by the Commission, or any member thereof, or its clerks, accountants or examiners at any time the Commission shall deem it advisable in the same manner as is provided for the examination of State banks, and requires the investment company to pay a fee for each of such examinations of not to exceed $7.00, "for each day or fraction thereof that any member of said Commission, clerk, accountant or examiner is absent from the capitol building for the purposes of making such examination," and also to pay the actual travelling and hotel expenses of the person or persons making such examination, and it provides that the failure or refusal of any investment company to pay such fees on demand of "such Commission, clerk, accountant or examiner, while making such examination" shall work a forfeiture of the right of that company to sell or offer for sale any of its contracts, stocks, bonds or other securities in the State of Michigan; fixes the same fee for a preliminary examination, as aforesaid, and enacts that "in case it shall be made to appear to the Commission from the examination of said investment company after said investment company has been

authorized to sell its stocks, bonds and securities," that the further sale thereof would work a fraud upon the purchaser, the Commission may by order revoke the license of the investment company to sell its stocks, bonds and securities, upon notice duly given and a hearing duly had, and may, pending such hearing, suspend the right of such company so to sell.

By Section 16, all information obtained by the Commission with reference to any securities and all the records of the Commission are made open to examination by the public.

By Section 20, provision is to be made to furnish those who may apply therefor, with information regarding any investment company or its affairs on file with the Commission.

By Section 21, every investment company, domestic or foreign, is required during the month of January in every year to file with the Commission a detailed statement in such form and giving such information as the Commission shall require, showing its condition at the close of business the preceding December 31st.

By Section 22, the Supreme Court is given jurisdiction upon petition of any person aggrieved, to review by certiorari any final order of determination of the Commission, but the issuance of the writ is not, unless specifically ordered by the Court, to operate as a stay of proceedings.

By Section 23, any person who shall violate any of the provisions of the Act shall be deemed guilty of a misdemeanor, and on conviction fined not more than $1,000 or imprisoned in the county jail for not more than one year in the discretion of the Court.

Section 24 provides that if the courts of the State

should declare any section or provision of the Act unconstitutional or unauthorized or in conflict with any other section or provision of the Act, then such decision shall affect only such section or provision so declared to be unconstitutional or unauthorized, and shall not affect any other section or part of this Act.

The other provisions of the Act and other sections not quoted refer to matters of machinery, and are not essential to the consideration of the points upon which the constitutionality of the Act depends.

Briefly, this act makes the right of a foreign or domestic corporation, or any purchaser from it of its stock or bonds, or of any agent employed to sell its stock or bonds, in the State of Michigan, to depend upon:

(1) Its first obtaining permission or license of the Commission, to secure which it must pay the fees, and furnish the information specified in Section 4; and (if a foreign corporation) must file an irrevocable consent to be sued in any county in Michigan in which a cause of action may arise, or in which the plaintiff may reside;

(2) its subjecting itself to the investigations described in Section 8, and the indefinite expense of examination of its affairs in Section 13, under penalty of forfeiture of its rights to sell its stock or bonds in Michigan, if it do not pay such expenses on demand;

(3) its subjecting itself to the control of the Commission as described in Section 8, as to the amount of bonds, stocks or other securities it may issue, and the liability to have those already issued cancelled.

It subjects its right to directly or indirectly market its stock or bonds in Michigan to forfeiture, in case the Commission shall be of the *opinion* that the sale of such stock or bonds would work a fraud upon the purchaser.

It makes the right of any individual, or corporation, to carry on the business of dealing in stocks or bonds of corporations in the State of Michigan dependent upon securing a license from the Commission, to obtain which he must

> register and furnish the information, and pay the fees, prescribed in Section 11, and (if a non-resident or foreign corporation) irrevocably *appoint* the Commissioner of the State Banking Department of Michigan his or its agent upon whom process against him or it may be served.

Besides, in every case of the sale or offer for sale of securities for which a certificate or license has not been given to the issuing company, the dealer must

> make application as provided in the case of the issuing corporation, and can obtain the certificate only when the conditions specified, including investigation and appraisal if desired, under Section 8, have been met.

This latter requirement on the dealer is prohibitive in many cases, potentially prohibitive, at the will of the Commission, in all cases.

Discussion of the Act.

We desire on this appeal to urge only what seem to us to be the fundamental defects of the present act. The whole act rests on four propositions:

1. That the right to buy and sell securities as a business, or "in the course of continued or successive transactions of a similar nature" may be prohibited except under executive license subject to revocation.

2. That the right to sell securities in a given case may be prohibited except under executive license subject to revocation.

3. That no securities can be sold in the State which have been issued for property "in excess of (its) value" as found by the Commission.

4. That exemption from the act may be obtained by listing a security in a standard manual approved by the Commission.

1. The licensing of the business is the pronounced feature of the Ohio Act. The control over each transaction is the pronounced feature of the Michigan Act. Both features are present in each act.

The Michigan, 1915, Act, does not in terms make the original license discretionary. It does require a regulative license fee of $50, and the furnishing "said Commission with such other information as said Commission shall deem necessary" as to the character of the dealer's business. This fee and these burdens are a prerequisite to the right of any dealer to sell a single bond in the State. As to at least one of the intervenors, Remick, Hodges & Co. (Supplemental Rec., p. 3) they are prohibitive.

The irrevocable appointment of the Banking Commissioner as an agent for service of process is also required. No duty of giving notice of such

service to the defendant is by the statute devolved upon that official.

The license "shall be good until revoked by said Commission for good cause upon notice to such dealer and a hearing duly had" (Section 11).

There is no specification defining the "*good cause*" for which a license may be revoked. The power of revocation is complete based on the assumption that the business is subject to prohibition and may be made dependent upon the sufferance of the Commission.

No securities whatever can be offered or sold of the non-exempt class covered by the license "unless and until said Commission has approved thereof and issued its certificates in accordance with the provisions of this Act" (Section 14).

This is the sweeping and fundamental prohibition of the act. It applies without chance of evasion to every offering by any dealer within or without the State, and to every security, wherever issued, offered or attempted to be offered in the State, except only those exempted under Section 3.

The only "certificate in accordance with the Act" is that provided for under Section 9. It may be obtained by the issuing company in the first instance, but if not so obtained, the dealer must obtain it at his own burden and expense. There is no escape from this prohibition. The dealer "shall make application to said Commission for license as hereinbefore provided for applications by investment companies and shall pay the same fee required to be paid by said investment companies."

The application by an investment company is under Section 4. Transposing the language to fit the dealer and putting upon it the most liberal construction, the dealer is required to file:

1. "A statement showing in full detail the plan upon which" the investment company "proposes to" or does "transact business."

2. "A copy of all contracts, stocks, bonds, or other instruments which" the dealer proposes to sell to his customers, "together with a copy of (his) prospectus, and of the proposed advertisements of (his) sale of stocks, bonds or other securities."

3. Such statement "shall also show the name and location and main office of the investment company; the names and addresses of its officers, and an itemized account of its financial condition, and the amount of its assets and liabilities, and such other information touching its condition and affairs as the Commission may require," also "all papers pertaining to its organization," including charter, State laws, etc.

4. A filing fee equal to 1/10 per cent. of the face value of the securities offered not exceeding $100 nor less than $10.

5. All papers verified by an officer of the corporation.

6. An irrevocable consent to service by a foreign investment company.

This latter requirement might be held not to apply when application is made by the dealer, though it evidences a purpose to secure jurisdiction over the issuing company as a necessary condition precedent to permitting its securities to be sold in the State.

These provisions are in effect completely prohibitive of the normal sale by a dealer of the securities of any company which has not itself

complied with the act. We say "the normal sale," meaning the sale by a dealer of securities which he has purchased in the normal way and desires to sell in the normal way. If he is making a flotation of an original issue acquired from the company and desires to float a substantial part of them in Michigan, he could presumably in the first instance, in some cases, obtain the proofs required and get the Commission's certificate. But if he was simply the owner of the securities and desired for his own account to sell them in Michigan, it cannot be assumed that he could compel or induce the investment company to give him all the data required by the act, or which might be required by the Commission.

No provision is made for waiving these provisions. The scheme of the act is plain to prohibit the sale of the securities of any company which does not furnish all the information required or desired.

But the foregoing is not all. The "certificate of authority" may be withheld until the Commission "may make or have made under its direction a detailed examination of such investment company's property, business and affairs, which examination shall be at the expense of such investment company. It may cause an appraisal "at the like expense of all its properties, tangible and intangible" (Section 8). If the dealer is applying, this expense and burden must fall upon him. If he does not feel able to pay it, he will not get the "certificate of authority" to sell his own property.

If upon the information filed and investigation made,

"The said Commission finds that the proposed plan of business of said investment company, or that its proposed contracts, stocks, bonds or other securities"

a. "are fraudulent or"

b. "are of such a nature that the sale" thereof "would in the opinion of the Commission work a fraud upon the purchaser"

"then said Commission shall disapprove the sale * * * and shall notify" such company, and it shall be unlawful for such company "to offer or sell the securities in the State, and said securities "shall not be sold in this State."

"If, however, said Commission shall not find" the conclusions so stated above (a or b),

"then it shall approve the sale of such *stocks*" (*sic*) in Michigan "and issue its certificate" in terms stating that has been given permission to sell $ of the given security in the State, and adding in type two sizes larger than any other part of said certificate, the words:

"The Commission does not recommend the purchase of this security."

The duty to use this warning only arises when under the act the Commission "shall approve the sale," a point worth much as a selling argument, it not being necessary to call the investor's attention to the further fact that this duty to "approve such sale" is mandatory upon a negative condition, the failure or inability of the Commission to find, if it "shall not find," that the sale is fraudulent or would work a fraud (Section 9).

3. But even though there be no fraud or prospect of fraud in law or in effect, the certificate may still be withheld. Last, but not least, the Commission

"may fix the amount" of securities to be issued for property and require such securities to be "deposited in escrow under such terms" as it prescribes, and may "withhold its license to sell" securities if they have been issued for property "in excess of (its) value as found by said Commission * * * until such * * * securities issued * * * in excess of the value so found by said Commission have been surrendered to such corporation and cancelled by it" (Section 8).

We would like to find some reasonable workable construction of this section, because we desire to test the fundamental principle involved in it, that the State can, through its Commission and upon its finding prohibit the sale in the State of stocks or bonds of a corporation of another State if the Commission disagrees with the judgment of the corporate officers, acting under authority of the State creating the corporation, and possibly upon the specific finding of officials of the issuing State, as to the value, for instance, of a patent for which stock has been issued.

In the argument in the Court below on the Michigan 1913 Act, it was very frankly conceded by the Attorney General that had that act been in force and enforced when the Ford Automobile Company was financed, that company and its automobile in all likelihood would not now be in existence. Nor did he find it necessary to apologize for such a law, but justified it by naming other concerns which have since failed, which he said would also have been made impossible. In reply it was pointed out by counsel familiar with the other concerns named, that they in their inception were very promising ventures, not like the Ford enterprise, a mere speculative possibility based on the intangible asset of a human brain.

Countless enterprises, including the greatest modern inventions, could be cited which, like the Ford automobile, might never have seen the light of day, had the power to finance them been subject to the veto of a State Board given by these acts.

The present Section 8, in fact takes the place of "*the probability of loss*" feature of the original act. There must in the opinion of the Commission be full face value back of the securities before they can be sold in Michigan at any price.

4. But all these drastic prohibitions mean nothing. These plaintiffs and intervenors have nothing to which to object and nothing to fear. Michigan dealers, we are told, have no trouble with the act, and outside dealers need have no trouble. Under Section 3, "the provisions of this act shall not apply to—(h) *securities which are listed in any standard manual of information approved by said Commission.*" Under Section 10, a man does not become a dealer when he offers securities "specially exempted in this Act," and under Section 11 he is not required to obtain a license or pay a fee unless he desires to sell "securities not exempted under the terms of this Act."

If a "standard manual" means anything to this Court, that is, if it takes judicial notice of what a standard manual is, it must, of course, have the correct knowledge as to it. It will not indulge in any assumption contrary to the fact, that the manual furnishes any specific security against fraud. It will know that these manuals publish such information as is available and that some if not all of them charge for listings, and that any person may secure the listing of any securities which are deemed to be of sufficient interest to be included.

The inclusion or exclusion of a particular security is within the discretion of the publisher. Upon its inclusion, the security becomes exempt from the act under consideration. The bill of complaint (Record, pages 10 and 11) gives a list of the manuals aproved by the Commission. We have before us Moody's Manual of Railroads, 1916, and find this statement in the preface:

> "While the figures and data contained in the manual have been obtained from sources believed to be reliable and accurate, the publishers do not hold themselves responsible for the accuracy of any of the statements contained therein."

Opening the book at random, we happen to note at page 1551:

> "Crooked Creek R. R. & Coal Co. (Independent)" incorporated 1875 in Iowa. "Line of road Webster City to Lehigh, Ia., 17.61 miles; sidings, etc., 3.45 miles * * * Equipment: Locomotive 1; cars (box 68; coal 18) 86.
>
> "Receiverships, etc. * * * Sam McClure of Fort Dodge, Ia. was appointed Receiver on or about July 25, 1915. * * *
>
> "Capital Stock—outstanding $112,500.
>
> "Bonded Debt $112,500—July 1, 1915, interest defaulted. * * *

	Deficit for year.
1910-11	$2339
1911-12	5160
1912-13	11,557
1913-14	1,133
1914-15	9,581."

It is a well known fact that most of the dealers affected by the law, especially the local dealers, do business under the manual plan, listing their securities when necessary in the so-called "Michi-

gan Manual of Corporation Statistics" mentioned in the bill of complaint (Rec., page 11).

The manual provision is "the Michigan idea" of providing an easy way out of the act at all times. It is not so much an exemption of existing standard securities, as a working exemption available for new offerings to be listed as issued.

The following proviso is attached to the provision exempting securities listed in approved manuals:

> "Provided, however, that said Commission shall have the power to call for additional and further information than that contained in such manuals, with reference to any securities listed therein, and may, pending the filing of such information, suspend the sale of such securities, and also suspend, either temporarily or permanently, the sale of any securities listed in such manuals after a hearing upon notice to the issuer of such securities if said Commission shall find that the sale of such securities would work a fraud upon the purchasers thereof."

There is nothing in the Act to indicate how the Commission are to learn that any particular security exempted under Section 3 is being offered in the State. Unfortunate indeed would be the position of a dealer with a block of Rock Island bonds if the sale thereof were permanently suspended "after a hearing upon notice to the issuer thereof." The importance of this plainly unconstitutional proviso lies in the fact that the exemption would not have been inserted without it, and that the Act would not have been adopted without the exemption.

Approach and Contact of Authorities.

1. *Arbitrary Power and Discretionary Authority Inadmissible.*

In *Yick Wo* v. *Hopkins,* 118 U. S., at page 370, the Court said that the principles of our institutions of government "do not mean to leave room for the play and action of purely personal and arbitrary power," adding:

> "* * * the fundamental rights to life, liberty, and the pursuit of happiness, considered as individual possessions, are secured by those maxims of constitutional law which are the monuments showing the victorious progress of the race in securing to men the blessings of civilization under the reign of just and equal laws, so that, in the famous language of the Massachusetts Bill of Rights, the government of the commonwealth 'may be a government of laws and not of men.' For, the very idea that one may be compelled to hold his life or the means of living, or any material right essential to the enjoyment of life, at the mere will of another, seems to be intolerable in any country where freedom prevails, as being the essence of slavery itself."

Mr. Justice Peckham in *Allgeyer* v. *Louisiana,* 165 U. S., 578, at page 589, said:

> "It was said by Mr. Justice Bradley in *Butchers' Union* v. *Crescent City Company,* 111 U. S., 746, 762, in the course of his concurring opinion in that case, that 'The right to follow any of the common occupations of life is an inalienable right.' It was formulated as such under the phrase 'pursuit of happiness' in the Declaration of Independence, which commenced with the fundamental proposition that 'all men are created equal, that they are endowed by their Creator with

> certain inalienable rights; that among these are life, liberty and the pursuit of happiness.' This right is a large ingredient in the civil liberty of the citizen. Again on page 764, the learned Justice said: 'I hold that the liberty of pursuit—the right to follow any of the ordinary callings of life—is one of the privileges of a citizen of the United States.' And again, on page 765: 'But if it does not abridge the privileges and immunities of a citizen of the United States to prohibit him from pursuing his chosen calling, and giving to others the exclusive right of pursuing it, it certainly does deprive him (to a certain extent) of his liberty; for it takes from him the freedom of adopting and following the pursuit which he prefers; which, as already intimated, is a material part of the liberty of the citizen.' It is true that these remarks were made in regard to questions of monopoly, but they well describe the rights which are covered by the word 'liberty' as contained in the Fourteenth Amendment."

In re Hollon Parker, 169 U. S., 221, Mr. Justice Field said (225):

> "Rights under our system of law and procedure do not rest in the discretionary power of any officer, judicial or otherwise."

2. *Administrative Control of Certain Matters Necessary.*

In *Lieberman* v. *Van de Carr*, 199 U. S., 552, the constitutionality was upheld of Section 66 of the New York Sanitary Code, which reads as follows:

> "No milk shall be received, held, kept, either for sale or delivered in the City of New York, without a permit in writing from the Board of Health, and subject to the conditions thereof."

The Court read the decision of the New York Court of Appeals as meaning that this provision was sustained as "the grant of power to issue or withold permits in the honest exercise of a reasonable discretion" (p. 559). The Court said, page 560:

> "That this Court will not interfere because the States have seen fit to give administrative discretion to local boards to grant or withhold licenses or permits to carry on trades or occupations, or perform acts which are properly the subject of regulation in the exercise of the reserved power of the States to protect the health and safety of its people there can be no doubt."

And further that cases which it cited and reviewed

> "* * * leave in no doubt the proposition that the conferring of discretionary power upon administrative boards to grant or withhold permission to carry on a trade or business which is the proper subject of regulation within the police power of the State is not violative of rights secured by the Fourteenth Amendment" (562).
>
> "* * * *If the business affected is one which may be properly the subject of such legislation*, it is no valid objection that similar legislation is not imposed on other businesses of a different kind."

In *Noble State Bank* v. *Haskell*, 219 U. S., 104, Holmes, J., expressed the opinion (p. 113) that the State control of banking "may go on from regulation to prohibition except upon such conditions as it may prescribe."

And in *Engel* v. *O'Malley*, 219 U. S., 128, in upholding the constitutionality of the New York statute of 1910, Chapter 348, forbidding individuals

or partnerships engaged in the business of receiving money for safe-keeping or transmission, from doing business without a license from the Comptroller, the Court pointed out that the business was one largely done by poor and ignorant immigrants, especially upon their first arrival here; that

> "* * * experience has shown that the protection of such depositors against fraud, which is the purpose running through the statute, is especially needed by at least that class of them with whom the persons hit by the statute largely deal. The case cited establishes that the State may regulate that business and may take strong measures to render it secure" (p. 136).

The Court said:

> "The power of the State to make the pursuit of a calling dependent upon obtaining a license is well established where safety seems to require it."

In *German-Alliance Insurance Co.* v. *Lewis*, 233 U. S., 389, a statute authorizing the Superintendent of Insurance to supervise and control the rates charged by fire insurance companies was upheld on the authority of *Munn* v. *Illinois* and *Budd* v. *New York*, on the ground that the insurance business was a business subject to regulation, no question being raised whatever as to its subjection to executive control for this purpose. The Court said (p. 414):

> "To the contention that the business is private we have opposed the conception of the public interests. We have shown that the business of insurance has very definite characteristics with a reach of influence and conse-

> quence beyond and different from that of the ordinary businesses of the commercial world, to pursue which a greater liberty may be asserted. The transactions of the latter are independent and individual, terminating in their effect with the instances. The contracts of insurance may be said to be interdependent. They cannot be regarded singly, or isolatedly, and the effect of their relation is to create a fund of assurance and credit, the companies becoming the depositories of the money of the insured, possessing great power thereby and charged with great responsibilities. * * * The principle we apply is definite and old and has, as we have pointed out, illustrating examples. And both by the expression of the principle and the citation of the examples we have tried to confine our decision to the regulation of the business of insurance, it having become 'clothed with a public interest' and, therefore, subject 'to be controlled by the public for the common good' ".

In *Brazee* v. *People of Michigan*, 241 U. S., 340, it was held that the State, in the exercise of its police power, may require licenses for employment agencies and prescribe reasonable regulations in respect to them to be enforced according to the legal discretion of a Commissioner, saying (p. 343):

> "The general nature of the business is such that unless regulated many persons may be exposed to misfortunes against which the Legislature can properly protect them."

See, also, prohibition or administrative control upheld in

> Austin *v.* Tennessee, 179 U. S., 343 (prohibiting sale of cigarettes).
>
> Gundling *v.* Chicago, 177 U. S., 183 (license for sale of cigarettes).

Wilson *v.* Eureka City, 173 U. S., 32 (address on public grounds).

Jacobson *v.* Massachusetts, 197 U. S., 11 (vaccination).

Fisher *v.* St. Louis, 194 U. S., 361 (Keeping cow stable within City limits).

Mugler *v.* Kansas, 123 U. S., 623 (Liquor Prohibition).

Giozza *v.* Tiernan, 148 U. S., 657 (Liquor License).

The cases cited illustrate the far-reaching character of the executive or administrative control which may be created over "a business clothed with a public interest." The prohibition or the control given may be complete and unqualified. The State "may go on from regulation to prohibition except upon such conditions as it may prescribe." A man may not do such business "without a permit" from a state board and "subject to the conditions thereof." The Legislature may grant or withhold this complete administrative power, it may prescribe standards or rules to control it, but whether it grants, withholds or conditions it, there is no question of its power to grant it completely; that is, there is no question of constitutional prohibition or of the separation of governmental powers or of the delegation of legislative powers. The power is historically and properly administrative, subject, as all powers, to protection against its "purely personal and arbitrary" exercise. This complete power may, we take it, be given over many matters, which, on one or more special and distinctive grounds, both require and are susceptible of such control, including many quasi-public businesses, and businesses involving special dangers to the public or to a community, as well as over government agencies and government

property, including parks, highways and navigable rivers, and matters of international character such as aliens and foreign commerce (see cases under Point III).

3. *Legislative Restrictions and Safeguards Proper.*

The cases above cited deal with administrative control over matters of public right or public grant or existing at public sufferance. The Legislature may deal drastically with many matters of private right, to prevent or redress individual wrongs. Drastic remedies may be prescribed *by law* for evils deemed by the Legislature to require them. These include "that wide department of activity which consists of the making of contracts," as to which "restrictive safeguards" may be required, for "liberty implies the absence of arbitrary restraint, not immunity from reasonable regulations and prohibitions" (Chicago, B. & Q. R. R. Co. *v.* McGuire, 219 U. S., 549, p. 567). It permits "legislation in the exercise of the police power which regulates the manner of the use or disposition of property" (Spurr *v.* Travis, 145 Mich., 721, p. 724; upholding the Michigan Bulk-Sales Act, sustained by this Court in Kidd *v.* Musselman, 217 U. S., 461).

In Brodnax *v.* Missouri, 219 U. S., 285, the Court upheld a statute of Missouri which prohibited the keeping of places for dealing in stocks, bonds and commodities for future delivery "without at the time of the sale the seller shall cause to be made a complete record of the things sold, the purchaser and the time of delivery in a book kept for that purpose," and deliver a written memorandum with a stamp affixed thereon.

In Otis *v.* Parker, 187 U. S., 606, the Court upheld a provision of the California constitution de-

claring void all contracts for the sale of stock on margin, and Holmes, J., said at page 610:

> "There is no doubt that purchases on margin may be and frequently are used as a means of gambling for a great gain or a loss of all one has."

See also similar statutes upheld in

Knoxville Iron Co. v. *Harbison,* 183 U. S., 13 (requiring redemption in cash of "pay scrip");

Rosenthal v. *New York,* 226 U. S., 260 (requiring second-hand dealers to make inquiry as to ownership);

Schmidinger v. *Chicago,* 226 U. S., 578 (prescribing size of loaves of bread);

Lemieux v. *Young,* 211 U. S., 489;

Plumley v. *Massachusetts,* 155 U. S., 461 (prohibiting sale of oleomargarine colored to resemble butter);

House v. *Mayes,* 219 U. S., 270 (requiring sales by actual weight without deduction under any custom or rule of any Board of Trade);

Savage *v.* Jones, 225 U. S., 501, and Patapsco, etc., Co. *v.* North Carolina, 171 U. S., 345, and other inspection cases. (Prohibiting the sale of products for special use not meeting prescribed standard determinable by physical inspection, or chemical analysis, all based on principle stated in Gibbons *v.* Ogden, 9 Wheat., 1, 203, and Turner *v.* Maryland, 137 U. S., 38.)

State v. *Holton,* 148 Iowa, 724 (requiring linseed oil to be labelled to prevent deception).

"The Statute of Frauds, the act to prevent fraudulent conveyances, insolvent laws, the Recording Act, the prohibition of usury, lien laws, regulations in relation to chattel mortgages, conditional sales and preferences by corporations and in general assignments, show in how many ways and in what varied forms the Legislature may properly restrain freedom of action in commercial transactions in order to promote the general welfare."

Vann, J., dissenting Opinion in Wright *v.* Hart, 182 N. Y., 330, 348.

Cited and approved in Lemieux *v.* Young, 211 U. S., 489, at 493, 495.

It is the contention of the appellees that whatever evil exists within the field covered by this Act falls within the general legislative power and should be dealt with on the principles and precedents of ordinary remedial legislation. That the business neither requires nor justifies, nor is susceptible of, administrative or executive control for the purpose of preventing a wrong or injury by one individual to another.

4. *Whether regulative or restrictive, legislation must not be plainly violative of constitutional rights.*

In *Gundling* v. *Chicago, supra,* Mr. Justice Peckham, at page 188, said:

"* * * unless the regulations are so utterly unreasonable and extravagant in their nature and purpose that the property and personal rights of the citizen are unneces-

sarily, and in a manner wholly arbitrary, interfered with or destroyed without due process of law, they do not extend beyond the power of the State to pass, and they form no subject for Federal interference."

In Lawton *v.* Steele, 152 U. S., 133, at page 137, it was said by Mr. Justice Brown:

> "To justify the State in thus interposing its authority in behalf of the public, it must appear, first, that the interests of the public generally as distinguished from those of a particular class, require such interference; and, second, that the means are reasonably necessary for the accomplishment of the purpose, and not unduly oppressive upon individuals. The Legislature may not, under the guise of protecting the public interests, arbitrarily interfere with private business, or impose unusual and unnecessary restrictions upon lawful occupations. In other words, its determination as to what is a proper exercise of its police powers is not final or conclusive, but is subject to the supervision of the Courts."

ORIGIN OF BLUE SKY LEGISLATION.

In his brief before the lower Court in the case involving the Michigan Act of 1913, the present Attorney General said:

> "Get-rich-quick schemes have sprung up all over the country; visionary oil wells, not gushing but just ready to gush, have been capitalized and sold in untold millions to the American people; gold mines upon paper of fabulous richness have been discovered (?) in every part of the civilized and uncivilized globe, capitalized for millions and the stock sold to the unsuspecting laboring man and farmer. Every conceivable scheme to separate the frugal from their money have been de-

> vised by the shrewd and cunning in their wild cat ventures. Michigan has not been alone in this dilemma. This Act is designed to put a stop to the seepage of untold millions from the pockets of the frugal to the pockets of the unscrupulous."

And in his present brief for appellant, he says, page 80:

> "The purpose of the Act here involved must be apparent to the Court, the purpose being that no one shall be permitted to sell in the State of Michigan and separate the people of the State from their money through the medium of fraudulent mining stocks, oil stocks and other fly-by-night ventures."

An extremely friendly student of this whole subject, Hon. Thomas Mulvey, Under Secretary of State of Canada, made an exhaustive investigation of it in 1913. We quote as follows from the printed report which he prepared for the State Department covering this investigation:

> "For the purpose of making a close investigation of the operation of the Kansas law I went to Topeka some months ago, and studied its operations in the office of the Banking Commission. I also discussed it with the Attorney General and the Secretary of State of Kansas and with many lawyers and business men of Topeka, Kansas City, Kansas; and Kansas City, Missouri.
>
> "Prior to the election in the State of Kansas preceding the last, Mr. J. N. Dolley was the Chairman of the Republican State Committee, and as he was a prominent merchant and president of a local savings bank, on the return of his party to office he was made Bank Commissioner. Mr. Dolley established a branch of his office for the purpose of investi-

gating securities offered generally throughout the State, and for the purpose of showing the advantage of the Department, gave the matter as great publicity as possible through the press, as shown by the following:

'STATE OF KANSAS
'Office of Bank Commissioner.

'J. N. Dolley,
'Bank Commissioner.

"Topeka, December 16, 1910.

'To the Editor:

'About one year ago the banking department organized a bureau to investigate the sale of stocks, bonds and other securities in Kansas. We have made much research along these lines, and are amazed at the enormous amount of money the Kansas people are being swindled out of by these fakers and 'blue-sky merchants.' I find that Kansas is literally infested with them.

'They are sitting around, and when a man dies the widow receives her pittance of insurance—one, two or three thousand dollars, as the case may be, mostly from fraternal insurance. These thieves show up a few days after the funeral and undertake to sell the widow some of their fake stock, promising her dividends of anywhere from fifteen to fifty per cent. per annum. They are getting a large amount of money from this source, as well as a great many other sources, and their victims are mostly those who are unacquainted with business methods, but are hard-working, frugal, saving people, and can ill afford to lose the money.

'I find that Kansas has been tolled millions and millions of dollars during the past few years by these confidence men, and ninety-eight per cent. of the money so paid has been entirely lost by the investor.

As near as I can ascertain, they are tolling Kansas at the rate of somewhere between one and three millions of dollars per annum. Scores of them have quickly packed their grips and left the State upon this department starting to look them up. I do not believe that there are one-third as many operating in Kansas today as there were one year ago, and I propose, through the newspapers, with publicity to drive every one of these thieves possible from our State. *I will ask the Legislature for a law clothing some department of State with the power to remove these financial cancers entirely from our State, and I am sure, with the proper help of the Legislature we can do so.*

'I sent the papers an announcement several months ago which they kindly published, warning their subscribers and I now wish to thank them for their kind assistance at that time. I enclose you a blank that I would like to have you print in your valuable paper, so that any one of your subscribers, if they wish information along these lines, may clip the same from your paper, fill it out and mail to this department, and I am sure we can give them some valuable advice and *be of much assistance to them in investing their money where it will not be lost.*

'I regret very much that I have no funds to pay you for this work and am obliged to ask you to do it gratis, but I know that you are interested in stopping this dishonest flow of money from Kansas and keep it within the State to develop our vast resources and at the same time protect your subscribers and the class of people who are being robbed, many of whom are helpless against the intrigues and dishonesty of these get-rich-quick vultures * * *.'

"Immediately after the passing of the Statute of 1911 Mr. Dolley commenced a cam-

paign of publicity of its terms and virtues, and I think it is due to him to state that there have been few if any Statutes which have been so thoroughly advertised through the press and magazines of the United States.

"Mr. Dolley in his first report of the operation of the Act, published 1st September, 1912, states as follows:

> 'The Department succeeded in getting the last Legislature to pass House Bill 906, commonly known as the Kansas "Blue-Sky" law, providing for the regulation and supervision of the sale of stocks, bonds, and other securities. This law, as you know, was something entirely new in the business world, but I am pleased to inform you that we have worked the same out in a very nice shape and accomplished some wonderful results. I estimate that it has saved the people of this State at least six million dollars since its enactment. Between fourteen and fifteen hundred companies have been investigated by this Department since the enactment of this law, and of this number less than one hundred have been granted permits to sell their securities in Kansas. The law is rapidly gaining fame all over the civilized world and I believe that a large number of the States will adopt a similar law at the coming sessions of their Legislatures. *I believe that a movement has been started that will eventually result in the regulation and supervision of all kinds of companies in the same manner as banks are now regulated and supervised.* There are a few minor amendments that should be made to this law, which I will be pleased to recommend to the Legislature at the proper time.'

"It will be noticed that Mr. Dolley states that 'between fourteen and fifteen hundred companies have been investigated by the Department, and that of this number less than

one hundred have been granted permits to sell securities.' A personal investigation of the files of the Bank Commissioners' office casts serious doubt upon the accuracy of this statement. All the officials of the office have been changed, and it is a matter of great difficulty to obtain reliable information upon the working of the Act. I may say, however, that the figures given to me by the Assistant Commissioner of Banking are as follows: Up to the 1st of April, 1913, permits were granted to forty-nine companies and refused to sixty-two. Permits were granted and subsequently cancelled in three cases, and the applications under the Act numbered about 1,600. It was further explained to me that Mr. Dolley's statement in his report that this large number was investigated means that that number of applications had been received and held for consideration. In the course of my inquiries, I ascertained that the Co-Operative Harvester Association, an Illinois company, applied for a permit to dispose of its securities to the extent of $700,000 in the State of Kansas, and that what was described as a 'temporary permit' given to it. There seems to be no provision in the Statute for such a permit, but I was informed that Mr. Dolley decided that the exigencies of the situation demanded that in order not to stop business such permits should be given. This company proceeded to sell its securities. Some time later, during correspondence between the company and the Bank Commissioner a point was reached at which the company refused to give additional information which the Bank Commissioner required, and the company decided to retire from the State. In the meantime, I am told that it had sold the greater portion of the securities for which they required a permit. The company is now in liquidation, and it is likely that all the capital invested will be lost. I was also informed of other cases where

temporary permits have been given and gross fraud has been perpetrated.

"I discussed the results of my investigation in conversation with Dr. H. A. Millis, Professor of Economics at the University of Kansas, at Lawrence, Kan., who had on several occasions checked the files of the office of the Banking Commissioner. He confirmed my results, with this exception, that the number of companies to which permits were given and permits refused are scarcely accurate, but the difference is so small as to be negligible in discussing the subject. It is apparent that the provision for investigation and permit was in effect inoperative, and it was a matter of surprise to find that with scarcely an exception the highest praise was given to this Statute by everyone with whom I discussed the subject, both at Kansas City, Mo., and Kansas City, Kan., and Topeka, Kan., the universal belief being that the number of fraudulent securities offered has been very largely decreased, and the character of the persons offering securities has been raised. *In my investigation I came to the conclusion that the clause of the Statute which required the vendors of securities to obtain a certificate from the Banking Commissioner is entitled to all the credit for that result.* The Statute was so widely advertised, and the statement that it was being stringently enforced became so widely circulated that vendors of questionable securities were frightened away. *If there is any virtue whatever in the Statute, it appears to me to be owing to this particular provision.* I may say that I discussed this deduction with several prominent lawyers in Kansas City and they agreed with my conclusion."

See also article by Mr. Mulvey in the American Economic Review of September, 1914. He quotes the following from the report of the British Board

of Trade, based on an investigation of this general subject in 1895:

> "Your committee may observe that they have dismissed from their consideration every suggestion for a public inquiry by the registrar or other official authority, into the soundness, good faith, and prospects of the undertaking at this or any other stage of the company's formation. To make any such investigation into the position of every new company complete or effectual would demand a very numerous staff of trained officers, and lead to great delay and expense, while an incomplete or perfunctory investigation would be worse than none. It would be an attempt to throw what ought to be the responsibility of the individual on the shoulders of the state, and would give a fictitious and unreal sense of security to the investor, and might also lead to grave abuses."

These quotations make it clear that the evil aimed at in this legislation was primarily that of the so-called get-rich-quick concerns promising enormous gains. They also make it clear that the Kansas Act was practically incapable of enforcement according to its terms and that as applied to concerns, the fraud of which was not obvious in the first instance the sanction of the state was given, with the result that large losses were sustained, presumably by the very class of investors sought to be protected, those who needed "assistance in investing their money where it will not be lost."

Despite the repeated generalizations as to the extent of loss through fraud in "get-rich-quick" securities, it is impossible to get from official or any other source a reliable estimate, even an approximate estimate, of actual losses. The statements published cannot be verified by those who

make them. Much less is it possible to ascertain to what extent such losses are due to fraud in the actual sale of securities. Many of these statements are attributed to the Post Office Deparment. But our inquiry at the Department for specific information has made it clear that it has issued none, and that there is none.

The reports of the Chief Inspector of the Department show many persons convicted, "charged with using the mails in furtherance of schemes to defraud," and estimates of losses from such frauds. But relatively few of them seem to be securities frauds. In one important item listed in the 1913 report as a stock selling-proposition involving an estimated loss of $6,000,000, what were really sold seem to have been "contracts" requiring monthly payments and providing for an ownership of one acre of land in Mexico. Including this typical case, the cases listed showed twelve "sale of stock" schemes, one "sale of bonds," one "guaranteeing stocks and bonds" and one "issuing of bonds in connection with irrigation schemes," out of a total of over 200 fraud cases resulting in 304 convictions. The figures for 1914 are similar.

The report for 1914 refers to the fact that "the activity of the department during the last year in the issuance of fraud orders has effected a saving to the public of hundreds of thousands of dollars." Possibly a printer's error has converted "hundreds of thousands" into the "hundreds of millions" mentioned in the recent opinion of the North Carolina Supreme Court in State *v.* Agey, cited by the appellants.

As against these estimates of losses in various "fake" schemes, a part of which are stock flotations, may be cited the fact that close to $2,000,000,000

in new securities are issued and that several more billions change hands every year.

There is not and has not been any charge that fraud is prevalent in this normal business.

Mention should be made of the causes of losses other than fraud which without doubt enter very largely into the loose estimates made by every one on this subject. These causes are as variable as the transactions in which they occur. One degree removed from fraud is the reckless optimism of the promoter who believes in his enterprise and without sufficient capital himself seeks other people's money to finance his hopes. The ultimate failure is frequently due to the inability to raise sufficient funds actually to carry through a potent[illegible] profitable venture. In other cases the enti[illegible]osition is unsound, but neither the promo[illegible]s associates have the business judgm[illegible]ne fact.

Professor Dewing's volur[illegible]ate Promotions and Reorganizatio[illegible]ublished in 1914, furnishes much food for thought to those studying this question. He makes quite clear the general proposition that a part of the losses in industrial securities are due to mistakes of financing or organization, but much the larger part to subsequent incompetence and bad management or misfortune in the operation of the company.

It cannot, we think, be assumed that any Legislature, by investigation or otherwise, could have ascertained more than is known among the best informed writers and students of this subject. It is more likely, and in fact quite evident from the legislation itself that they did not even ascertain this, but acted upon the general popular misinformation, confusing fraud in the sale of securities with fraud in the operation of the business, and

magnifying many times the actual importance of fraud as a cause of loss in securities.

The Court will take judicial notice of the general course of business known to intelligent men.

The Normal Business Affected by Blue Sky Legislation.

The "Blue Sky" evil intended to be reached by this legislation is, as we have seen, that of the "Blue Sky merchant" and "fly-by-night" promoter of "get-rich-quick" enterprises. As the lower Court said in the first Michigan decision:

> "If just this intent had been carried into effect by the act as passed, these cases would not be here; but scrutiny of the law discloses additional and very different effects; it is not confined to corporations, but covers partnerships issuing, and individuals dealing in, securities; it does not relate alone to stocks, but as well to bonds, mortgages, and promissory notes; it is not limited to investment companies, as that term would ordinarily be defined, but extends the definition so that it may include most of the private corporations and partnerships in the United States; it does not cover fraudulent securities merely, but reaches and prohibits the sale of securities that are honest, valid, and safe; it does not simply protect the unwary citizen against fraudulent misleading, but it prevents the experienced investor from deliberately assisting an enterprise which he thinks gives sufficient promise of gain to offset the risk of loss, or which, from motives of pride, sympahy, or charity, he is willing to aid, notwithstanding a probability that his investment will prove unprofitable. Of course, not all of these results always follow; but some of them always may, and sometimes will. Take concrete instances. A merchandising partnership cannot borrow

additional capital from its home bankers on long time notes (over nine months) unless the Commission approves. If a timber company is insolvent, no one can deal in its first mortgage or underlying bonds, though these bonds are perfectly good, are not in default and not likely to be, nor can the Commission permit such dealing if it would. A successful automobile or furniture company may not increase and sell its capital stock, save by the Commission's approval, and, if such a company has not been successful and the Commission thinks it is not likely to be, the company must liquidate; it will not be permitted to get new capital. If a company is organized to make and sell a new invention, and if the Commission thinks the enterprise will not succeed the stock may not be sold, even to skilled bankers who have investigated thoroughly and still desire to buy. If, through local pride or in the effort to save an existing investment or from any indirect benefit to come, the citizens of a town wish to take stock or bonds in a local company, though knowing they are likely to lose their investment and being willing to take the chance, yet they may not; this law forbids."

Alabama & N. O. T. Co. et al. v. *Doyle et al.*, 210 Fed. Rep., 173, 175.

The present act is different in detail, but not in principle from the 1913 Michigan Act referred to by the Court. The business and transactions which it covers are not, in any definitive sense, connected with the Blue Sky evil. That evil is included in the broad generalities of the act, just as it would be included in any act dealing with the purchase and sale of property generally. The act covers expressly and prohibitively the borrowing or raising of money by stocks, bonds or secured or

non-negotiable notes by any person, partnership or company (except approved utility securities), and the entire business of buying and selling any such securities and the individual transactions involved in the continued or successive offer and sale of securities. Securities listed in so-called standard manuals are exempted from the primary prohibitions of the Act, but are subject at any time to prohibition by the Commission.

The Act covers, first, the future purchase and sale of billions of investment securities outstanding when it took effect. Whatever evils existed in the issuance of a small part of these outstanding securities was beyond remedy when the act was adopted. The securities themselves were lawful property rights.

The act covers, second, securities hereafter issued and which may become the subject of offer or sale within the State. Normally most of these securities would be issued in and under the laws of other States and become the property of individuals and companies, both within and without the State, before they came to be offered directly in the State. Here also any evils incident to the issuing of securities are beyond remedy when the securities come into the State. Here also the securities are the property of those who own and wish to sell them in the States.

The business concerns affected by the act are the investment dealers or so-called "investment bankers," numbering many hundreds, some of them very large houses with branch or allied houses in many cities of the country; others are relatively small but do a large aggregate business throughout the country. The business is essentially competitive.

The larger part of the business is normally interstate, carried on by houses in ten to twenty of the largest cities of the country. These houses buy and sell securities on their own account. They buy primarily for distribution to investors. They have an established clientele with whom they deal by mail or through agents. The total of this business must be at least a hundred times as large as the "get-rich-quick" dealings which are the professed object of this legislation. A large part of this business consists of the purchase of original issues of securities from the issuing company, after an exhaustive investigation by engineering, industrial and legal experts.

In all that has been said and written in litigation and in legislation in the past three years, it has, we believe, been nowhere suggested that there is in this normal business any abnormal degree of fraud.

This normal business is an investment business. The securities sold have no speculative feature in the sense of promising anything above a normal return or increase of value.

Unlike the speculative promotions, this business is normally carried on on a relatively moderate profit, a profit that could not hope to stand the expense involved in any serious effort by particular States to duplicate, each for itself, the expert examination necessary to protect the public against an assumed fraud.

These considerations are so fundamental that the idea of actually exercising the power given by the Blue Sky Acts against this normal business has been deprecated by the State officials themselves. They practically elect to ignore the acts and to accept the offerings of the established

houses on faith. But for this fact, the Blue Sky laws would undoubtedly be completely destructive of this business.

It should be added that, despite the fact that these laws have not been enforced according to their terms, they have in a substantial degree hindered and destroyed the normal business, particularly between the States. They have tended also to throw the business into the hands of resident houses, licensed in the particular State. If they are upheld and enforced, these effects will undoubtedly be farreaching and disastrous, both upon the interstate business as such and upon the present wide distribution of securities which is vital to our industrial and financial welfare.

Blue Sky Legislation.

As stated by Mr. Mulvey, the original Kansas Act of 1911 was widely if not altogether accurately advertised, and was followed in 1913 by a number of statutes, which are cited in appellants' brief. It is not correct, however, to say that these statutes were all based on the Kansas Act or all similar to it.

Blue sky bills were vetoed in Indiana and Colorado in 1913 and defeated by referendum in Washington in 1915. The Attorney General of Indiana in a sweeping opinion advised the Governor that the bill was unconstitutional, citing Baltimore, &c., R. R. *v.* Voight, 176 U. S., 498, and, referring to the sanction given by the State to an undetected fraud, added that "the bill, instead of assisting to close the door against fraud, would tend to throw it wide open and aid the fraudulent dealer to secure his victim's money."

The Kansas Act, apparently without any prior intention, went far beyond its professed pur-

pose of reaching the get-rich-quick concerns, and instead of dealing effectively with an exceptional class of dangerous business, practically subjected every transaction of purchase and sale of securities to prohibitions and provisions in terms completely unworkable and destructive of the normal business. Without making any distinction between the business concern issuing notes, bonds or stocks, and the dealer in or owner selling securities, classing them all as "investment companies," it prohibited every transaction unless the issuer or seller submitted a mass of specified detail and obtained in advance the approval of the Bank Commissioner based upon a detailed investigation of its or his financial condition and proposed contract, and placed itself or himself under the continued supervision and life-and-death power of the Commission. The assumption seemed to be that all securities were sold only by an issuing promoter. It or he, the promoter, dealer or seller covered by the Act, was required to pay a filing fee of $25 and was only permitted to sell securities that were approved upon a finding of his solvency, and that the "proposed plan of business and proposed contracts, contained and provided for a fair, just and equitable plan for the transaction of business and * * * promises a fair return on the stocks, bonds, contracts or other securities by it offered for sale."

The Kansas Act in its inception, as enforced, was simply a club with which the Bank Commissioner, when and as he chose, could drive any dealer from the State. Such was its value and its efficiency. Its harm and its inefficiency lay in the instances mentioned by Mr. Mulvey. These were not advertised or generally known, outside of Kansas, in 1913.

These crude provisions found their way in one form or another into the statutes of a number of States. *The fact that an Act as crude and completely unworkable as the Kansas Act was copied literally in so many states with equally crude changes in some, speaks volumes for the lack of any intelligent demand or interest in the subject.* In Michigan and Iowa, as in other states, efforts were made to so adjust the law to the facts as to permit legitimate business to be carried on, but owing to the fact that a violation of the Michigan Act was declared to be a felony, and to the fact that under the Iowa Act a bond in the sum of $5,000 was required, to be given conditioned upon a "strict compliance" with the Act, it seemed unsafe for legitimate dealers to attempt to carry on business under them, even though the officials charged with the enforcement of the Acts seemed desirous of waiving their drastic provisions. Suits were accordingly brought to contest the constitutionality of those two Acts, with the result that they were declared unconstitutional in the cases cited below.

Following the Michigan and Iowa decisions, a general discussion of the subject took place at the 1914 convention of the National Association of Supervisors of State Banks, whose members, we believe, included most of the State officials having charge of the actual enforcement of the laws. In this discussion the new Kansas Commissioner stated that "get-rich-quick" securities so-called are not offered in Kansas. They are kept out by the mere fact that we have such a law." Other officials deprecated various features of the laws, noting specially the dangerous sanction which it gave to "ap-

proved securities." The printed report of the convention is, we believe, available (pp. 47-59).

Upon the invitation of the abovenamed Association the Investment Bankers Association of America, which had participated in the attacks upon the Michigan and Iowa Acts, was represented at this discussion by its counsel, who urged that the "get-rich-quick evil should be met by constructive legislation directed against fraud in the sale of securities, and requiring specific safeguards to insure the effective investigation and prosecution of such frauds (pp. 35-44). A resolution was unanimously adopted under which a committee was appointed to "co-operate with the so-called investment bankers to secure uniform laws which will be practical in effect" (p. 116).

This Committee presented a form of fraud act at the 1915 convention of the same Association, which is printed with the proceedings of that convention (Report, pp. 53,54; Act, pp. 121-123). We print it, with the Committee's report as an appendix to this brief.

The Courts below have seemed to feel, and this Court may feel, quite properly, that we should be able to present some plan of act to demonstrate that the "get-rich-quick" evil can be met without resort to legislation of the present character. We point to the Bank Supervisors' Act, the Virginia 1916 Act (P. L. 835), and the Louisiana "itinerant agent" act (Laws 1912, Act 40).

A letter from the Attorney-General of Michigan was read at the 1914 convention of the Bank Supervisors' Association, in which he expressed the view that the decision in the *Doyle* case, *infra*, was unsound, and that "the general scheme of the Michigan Law to my mind is the proper scheme to

be worked out." Three months later the 1914 convention of the Attorneys General Association was held in Washington. The retiring President of the Bank Supervisors Association, the Bank Superintendent of Michigan, endeavored to arrange through the Attorney General of Michigan for a further discussion of the subject at the convention of the Attorneys General Association. This effort was unsuccessful, and at the latter convention, we understand upon the instance of the Attorney General of Michigan, and without any discussion of the subject, a Committee was appointed, consisting of the Attorneys General of Michigan, Iowa, and Arkansas, all of whom had been active in defence of the 1913 Acts. A further effort was made to cooperate with this Committee, but without the least success. Just as the Legislatures met in 1915, this Committee presented a form of act which with unimportant changes was immediately adopted in Michigan, and two or three other States, though not in Iowa. This Act represented apparently the work and views of the Attorney General of Michigan, and was, as he had forecast, based upon the 1913 Michigan Act.

This is the Act now before the Court.

Revised acts were also adopted in Iowa, Oregon, West Virginia, Kansas and North Dakota, entirely different from the Michigan Act. No new acts seem to have been adopted in any new States. The Wisconsin Act has been amended in 1916, doing away with the licensing of dealers, apparently on the view that it is unconstitutional and also unnecessary (Citations on Appellant's Brief, pp. 94-95).

Principle at Stake.

The principle of all this legislation is the same. The law of the land" is to be the will of the executive, telling one man to do, another not to do, a particular thing. It rests on *"the opinion"* of an administrative board or officer based on his own investigation as to the motive, character, or probable outcome of the private transactions of the individual. Some popular leaders and some Legislatures believe this principle to be constitutional. Some magazine writers have so assured them, and some lawyers have cited *dicta* from some decisions to support the view. The exception is said to be the rule, and established theories of government are said to have been abandoned.

The answer of course rests with this great Court. If we read aright its former decisions, they contain no authority for the widespread view that the conduct of any and all transactions of the business world may be subjected to the discretionary control of Boards or Commissions. The application of such government to different forms of quasi-public business has, we submit, represented not a change in the law, nor an extension of the executive power, but a change in the condition subject to the law and an application of that power to the changed conditions. The license and control of the village hack driver has been, not extended, but applied to the regulation of our great railroads. The control over banks has been, not extended, but applied to insurance companies and building and loan associations.

This development of legislation is largely a matter of the last five years. This is, we believe, the first case that has reached this Court, involving the

constitutionality of this principle of executive control over private business and individual transactions. Taking the view we do, we may be pardoned if we seem to exaggerate the importance of this case, and for the thought that the decision, one way or the other, must be epochal in its effect on the future government of the states and nation. We find ourselves entirely opposed to the popular view held by many lawyers, that this Court, has changed or will change the principles that have guided it in the interpretation of the Constitutional safeguards of the individual.

The Blue Sky Decisions.

There have now been a number of decisions in connection with the so-called "blue-sky" acts. In but six cases, however, has the constitutionality of such acts been really decided, and in each such case the Act has been held unconstitutional. These decisions cover the former Michigan, Iowa and West Virginia statutes, and the 1915 Michigan and South Dakota Acts, and the 1913 Ohio Act as amended. The West Virginia decision practically covered the original Kansas Act and those of other states based upon it. Fourteen Federal Judges five Circuit and nine District Judges, have now concurred in the opinion of the Court on the former Michigan Act and there has been no expressed dissent to that view.

The opinion in Alabama Trans. Co. *v.* Doyle 210 Fed., 173 (Sixth Circuit, Denison, C. J.; Sessions and Tuttle, D. JJ., all concurring), was cited and followed in Compton Co. *v.* Allen, 216 Fed., 537 (Eighth Circuit, Smith, C. J., McPherson and Pollock, D. JJ., all concurring).

And in Bracey *v.* Darst, 218 Fed., 482 (Fourth

Circuit), Dayton, D. J., Pritchard, C. J., concurring, after distinguishing *ex parte* Taylor, *infra*, discussing the statutes of several States, and construing the Act in the light of the Michigan and Iowa cases, concluded with the statement (496):

> "The opinions in the Iowa and Michigan cases are so clear, sound and convincing as to not only command our admiration, but lead us to the conclusion that nothing more complete and effective can be added to them."

The dissenting opinion of Circuit Judge Wood was based on a construction of the West Virginia Act, which took it out of the category of the other Acts, making it apply apparently only to corporations and those organized combinations of individuals whose business is "to raise money by the sale of the securities of such an organization to the public—that is to anyone who will buy." This construction in the opinion of the majority practically rewrote the statute. Referring to the Federal Court decisions on the Michigan and Iowa Acts, Judge Wood, simply said (502):

> "The statutes as construed in these opinions are more restrictive of the sale of securities than we find the West Virginia statutes to be."

In the case of Sioux Falls, etc., Co. *v.* Caldwell, now before this Court, reported in a footnote to the Ohio case (230 Fed., 236), the Federal Court (Judges Sanborn, Munger and Elliott) granted a restraining order *pendente lite*, the order reciting that

> "in the opinion of the Court, Chapter 275 of the Session Laws of the State of South Dakota for the year 1915, is violative of the Constitution of the United States, and this

> opinion is confirmed by the decisions in Alabama & N. O. Transportation Co. *v.* Doyle (D. C.), 210 Fed., 173; Wm. R. Compton Co. *v.* Allen *et al.* (D. C.), 216 Fed., 537 and Bracey *v.* Darst (C. D.), 218 Fed., 482."

This was followed by the decision of the lower Court on the 1915 Michigan Act, Judges Denison, Sessions and Tuttle, (228 Fed., 805), and by the decision on the Ohio Act, Judges Warrington, Sater and Hollister, (230 Fed., 233), both of which are now before this Court.

The other decisions are the following:

Ex parte Taylor, 66 So., 292 (Fla.), which upheld the Florida Act, the Act applying only to corporations selling their own securities, upon the power of the State "to limit and regulate the powers and operations of corporations which it brings into existence" (see West Virginia opinion, *supra*, discussing Taylor case).

Mechanics B. & L. Assn. *v.* Coffman, 110 Ark., 269, 162 S. W., 1090, in which the State Supreme Court upheld the former Arkansas Act, attacked at the suit of a building and loan association, solely on the ground that a building and loan association is subject to regulation.

Standard Home Co. *v.* Davis, 217 Fed., 904 (8th Circuit, Trieber, D. J.), in which the former Arkansas Act was attacked at the suit of a land-contract company. The Court dismissed the bill, saying in part (914, 915):

> "It is a well settled rule of law that a statute will not be declared unconstitutional at the instance of one not affected by it * * * The allegations in the bill, as set out in the statement of facts, show the complainant is not engaged in the sale of stocks, bonds,

> or other securities, as were the complainants in Alabama, etc., Transportation Co. *v.* Doyle (D. C.), 210 Fed., 173 (construing the Michigan 'blue sky' Statute), and in William R. Compton Co. *v.* Allen, 216 Fed., 537, decided by the District Court of the United States for the Southern District of Iowa (involving the Iowa Statute). Therefore these cases are not applicable to the instant case."

State *v.* Agey, 88 S. E., 726, which upheld the North Carolina Act of 1913, as applying to a concern similar to that as to which the former Arkansas Act was upheld.

We repeat, therefore, that nowhere in the lower Federal Court or in the Supreme Courts of any of the States, has there been any dissent by even a single judge to the principle announced in the first Michigan case, holding the Act void as applied to ordinary dealers in investment securities.

POINTS.

I.

The appellees are entitled to sue in equity to prevent "unlawful interference by criminal proceedings" against their agents, which would destroy their property and business.

II.

One who "in the course of continued or successive transactions of a similar nature" offers or sells stocks, bonds or other securities owned by him, cannot be prohibited from continuing such "business" except under executive license, subject to revocation.

III.

One who "in the course of continued or successive transactions of a similar nature" offers or sells securities owned by him, cannot be prohibited from making a particular offering or sale, except upon "certificate of authority" from a State Commission.

IV.

The so-called Standard Manual Feature of Act is unconstitutional and void.

V.

"The regulations are so utterly unreasonable and extravagant in their nature and purpose that the property and personal rights of the citizen are unnecessarily and in a manner wholly arbitrarily interfered with or destroyed without due process of law."

VI.

The act impairs the freedom of commerce between the states.

POINT I.

The plaintiffs are entitled to sue in equity to prevent "unlawful interference by criminal proceedings" which would destroy their property and business.

Ex parte Young, 209 U. S., 123.
Ludwig v. *Western Union Tel. Co.,* 216 U. S., 146.
Western Union Tel. Co. v. *Andrews, ibid.,* 165.
Herndon v. *Chicago R. I. & P. R. Co.,* 218 U. S., 135.
Missouri P. Ry. Co. v. *Tucker,* 230 U. S., 337.
Dobbins v. *Los Angeles,* 195 U. S., 223, 241.

The objection to the jurisdiction was urged in the Court below and is covered by the assignments.

In the *Young* case, the Attorney General of the State petitioned for writ of *habeas corpus* to be released from custody, being under arrest for disobeying an order enjoining him from instituting certain criminal proceedings under a State statute. The petition was dismissed, and the proceedings below sustained, and it was held that the Federal Court had undoubted power to restrain the enforcement of the State law, the Court saying (146):

> "The result would be a denial of any hearing to the company. The observations upon a similar question, made by Mr. Justice Brewer in *Cotting* v. *Kansas City Stock Yards Co.,* 183 U. S., 79, * * * are very apt. At page 100 he stated: 'Do the laws secure to an individual an equal

protection when he is allowed to come into Court and make his claim or defense, subject to the condition that upon a failure to make good that claim or defense, the penalty for such failure either appropriates all his property or subjects him to extravagant and unreasonable loss?' Again, at page 102, he says: * * * 'But when the Legislature, in an effort to prevent any inquiry of the validity of a particular statute, so burdens any challenge thereof in the Courts that the party affected is necessarily constrained to submit rather than take the chances of the penalties imposed, then it becomes a serious question whether the party is not deprived of the equal protection of the law.'

* * * * * *

"We hold, therefore, that the provisions of the acts relating to the enforcement of the rates, either for freight or passengers, by imposing such enormous fines and possible imprisonment as a result of an unsuccessful effort to test the validity of the laws themselves, are unconstitutional on their face, without regard to the question of the insufficiency of those rates. We also hold that the Circuit Court had jurisdiction under the cases already cited (and it was therefore its duty) to inquire whether the rates permitted by these acts or orders were too low and therefore confiscatory, and, if so held, that the Court then had jurisdiction to permanently enjoin the railroad company from putting them in force, and that it also had power, while the inquiry was pending, to grant a temporary injunction to the same effect.

* * * * * *

"* * * It would be an injury to complainant to harass it with a multiplicity of suits or litigation generally in an endeavor to enforce penalties under an unconstitutional

> enactment, and to prevent it ought to be within the jurisdiction of a court of equity. If the question of unconstitutionality, with reference, at least, to the Federal Constitution, be first raised in a Federal Court, that Court, as we think is shown by the authorities cited hereafter, has the right to decide it, to the exclusion of all other Courts.
>
> * * * * * *
>
> "Another obstacle to making the test on the part of the company might be to find an agent or employee who would disobey the law, with a possible fine and imprisonment staring him in the face if the act should be held valid."

In the *Ludwig* case, the Court affirmed a decree below enjoining the threatened proclamation by the Secretary of State under a State statute that the company was forbidden to do local business within the State. And in the *Western Union Telegraph Company* case, following it, argued and decided at the same time, the Court reversed a decree below dismissing the bill against the prosecuting attorney to enjoin him from bringing an action to recover penalties under the same act, saying (166):

> "It is averred in the bill, and admitted by the demurrer, that they threatened and were about to commence proceedings for that purpose. The unconstitutionality of the act is averred, and relief is sought against its enforcement. As this case is ruled upon the question of jurisdiction by the case of *ex parte Young*, it is unnecessary to consider the question further."

In the *Herndon* case, the Court affirmed a decree enjoining the prosecuting attorney from enforcing the penalties of a State statute, and restraining the Secretary of State from revoking the complainant's right to do business, saying:

"The bill avers that Harry T. Herndon, as prosecuting attorney for the County of Clinton, Missouri, threatens to and it will, unless enjoined, put in motion the special provisions of the Act of March 19, 1907, for the enforcement of penalties of $25 per day since July 21, 1907, which penalties in a short time would amount to many thousands of dollars. * * * As to the objection that the suit is one against the State, we think no discussion is necessary, and content ourselves with a reference to the late cases in this Court to that point."

Citing,

Ex parte Young, and
Western Union v. *Andrews*, *supra*.

In the *Dobbins* case, the Court restrained the enforcement of an ordinance preventing the erection of a gas works in the territory including plaintiff's premises upon which a gas works was in course of erection. The proceedings taken by the city and restrained by the act, involved simply *the arrest of employees*, the effect being to prevent the completion of the buildings. The Court said, referring to the efforts of the plaintiff to complete the building (241):

"She had the right to proceed with the prosecution of the work without interference by the city authorities in the form of arrest and prosecution of those in her employ.

"It is well settled that where property rights will be destroyed, *unlawful interference by criminal proceedings* under a void law or ordinance may be reached and controlled by a decree of a court of equity (Davis & Farnum Mfg. Co. *v.* Los Angeles, 189 U. S., 207, 218, and cases therein cited)."

POINT II.

One who "in the course of continued or successive transactions of a similar nature" offers or sells stocks, bonds or other securities owned by him, cannot be prohibited from continuing such "business" except under executive license, subject to revocation.

For the purpose of this brief we accept the definition of the act as confining its operation to those actually engaged as dealers in the business of buying and selling securities. We emphasize, however, the fact that it applies to dealers, as distinguished from brokers, and that by dealers we mean those who for a livelihood purchase and sell securities on their own account. This "business" is in its essence nothing more nor less than what is defined in the present act, the purchase and sale of securities "in the course of continued and successive transactions of a similar nature". It is simply the relative status of the active trader as compared with the occasional vendor. Neither in theory nor in practice is there any defined line between the individual who becomes more and more active in buying and selling investment or other securities, and the individual, partnership or corporate house that has acquired a clientele and buys for re-sale to investors. In its every act and aspect, the business represents simply a varying number of transactions, each of which is an individual transaction and a matter of individual right. The issuance of securities, especially of stock, by a business corporation presents a different question with which we are not now concerned, athough the issuance of notes and bonds by a partnership and, we think, by a private corporation, is merely a borrowing

of money, also "a varying number of transactions each of which is an individual transaction and a matter of individual right."

1. "The issuing * * * of stocks or bonds by a private company to get money for its own business no one can suppose is a public or quasi-public enterprise; the business of buying and selling stocks and bonds and other securities is no more 'affected by a public interest' than is the business of buying and selling groceries."

Per Curiam, in the Doyle Case, 210 Fed., 173, 179.

This is clearly the sound normal view of the normal business. Does the existence of "fly-by night" peddlers of oil and mining stocks change the normal character of this normal business?

Against the right to carry on this business the act in question is in principle, and to a large extent in fact, prohibitive.

"The object of a license is to confer a right that does not exist without a license; and, consequently, a power to license involves, in the exercise of it, a power to prohibit under pain of penalty without a license."

Chilvers *v.* People, 11 Mich., 43, p. 49.

The Court adding that

> "* * * The fact that a license is required to do an act is of itself a prohibition of such act without a license."

The professed aim of "blue-sky" legislation is to eliminate the "get-rich-quick" fakirs. The present act by its terms is directed against

the great normal business and the bulk of individual transactions involving the sale and re-sale of outstanding securities amounting to billions of dollars in amount. No effort whatever has been made to confine its operation to securities promising fabulous returns or sold by itinerant "fly-by-nights," or otherwise involving elements suggestive of fraud and danger. It includes the "get-rich-quick" promoter in the same way that an act directed against the purchase and sale of any wearing apparel would include the street peddler in paper collars. The exemptions from the act include certain investment securities, but they do not in any distinctive way exclude from the act the normal investment securities as such nor confine the operation of the act to peddlers of "get-rich-quick" securities as such. Its validity must be determined by its prohibition, not by its exemptions, unless it is clear that the prohibition is in fact confined to a class of transactions as to which it is constitutional. This is clearly not so. The normal business of appellees is included within its prohibition and is a business not properly subject to prohibition.

There has nowhere at any time been any suggestion of any wide-spread fraud in the sale or distribution of so-called investment securities. There are in fact many businesses where fraud is supposed to be more prevalent, including as instances horse trading and the automobile business. In practically every contractual transaction fraud is possible, and its prevention a proper subject for legislative action. If, upon a legislative assumption of the prevalence of fraud in any general business (as distinguished from a limited or special method of doing business) the entire business and

the right to carry it on may be made the subject of discretionary executive license, then no business can be judicially protected from the assertion of this power.

The subjection of certain business to executive license and control rests in many cases on usage and common assent running far back into the English law. There has never been any absolute individual right to engage in any of them. The modern trend of decisions is, we believe, toward a fuller protection of the public interests against the private interests asserting such right. These are the modern instances resting on ancient principle applied, it may be, to a wider field because of the more extended scope of modern business. The control of the village hackdriver has been applied to the transcontinental railroad, but there has been no change in the principle upon which it is founded.

Equally ancient and fundamental is the liberty of the individual to carry on his every-day transactions and "the right to follow any of the common occupations of life," subject only to "the law of the land." This liberty and right cannot be made the subject of an executive permit. It cannot be converted into a privilege subject to executive grant. This liberty and right are inherent in the individual—to put it strongly—so long as he is not in jail. Were the rule otherwise, could a man, for instance, deemed to be of ill repute be deprived of the right to follow an ordinary occupation, he would be in fact deprived of every occupation except fraud and crime. A convict who had served his term would be doomed for life to legal outlawry.

> "And a freeman may buy and sell at his pleasure. This right is not of society, but from

> *nature.* He never gave it up. It would be amusing to see a man hunting through our law books for authority to buy or sell or to make a bargain. The search would be vain."
>
> Arrowsmith *v.* Burlingim, 4 McLean, 489, 497.

The liberty of the individual, his right to engage in a vocation or calling as such, cannot be made the subject of executive control. The subjection to such control deprives him at once of his liberty and free use and disposition of his property. Even though the executive master may be a beneficent one, he is still a master and the individual has lost his liberty and the right to dispose of his property.

2. So far as we have been able to discover, no case has ever reached this Court where the power of executive license was asserted except against a business clearly subject to the power of prohibition. Many such cases have, however, been before the State Courts and the Acts held unconstitutional. Both the authority and reasoning of some of them are of value.

Under the Michigan Constitution as construed by the Supreme Court of the State, such an act is invalid.

In *People* v. *Berrien*, 124 Michigan, 664, the Court holding unconstitutional an Act requiring commission merchants *to obtain a license and give a bond*, said (666):

> "The business of buying and selling on commission has existed ever since commerce began. There are and always have been dishonest men engaged in it, as there are and always have been in every other branch of business. There are and always have

> been dishonest sellers, who will pack their produce in such a manner as to deceive. * * * There is no more reason why a commission merchant should pay a license fee, and execute a bond to pay his debts and to do his business honestly, than there is that any other merchant should pay a like fee, and file a like bond to properly do his business and pay his debts. The business requires no regulation, any more than any other mercantile pursuit. * * * It is not like a liquor traffic, which under the decisions of every Court, is subject to the police power, because of the injury it does to the health, morals and peace of the community, and may be prohibited altogether. Neither is there anything in it requiring regulation, as do hack drivers, peddlers, keepers of pawnshops and the like."

In *People* v. *Warden*, 157 N. Y., 116, at page 123, Chief Judge Parker said:

> "The tendency of the times undoubtedly is to rush to the legislature for a cure for all the grievances of citizens, whether real or imaginary, and many novel experiments are the result. *But usually in case of wrongs penalties have been provided.* It is novel legislation indeed that attempts to take away from all the people the right to conduct a given business because there are wrongdoers in it from whose conduct the people suffer."

In the recent case of *People* v. *Jenkins*, 202 N. Y., 53, holding unconstitutional an Act requiring a license of transient retail dealers selling in a store articles advertised as purchased at a bankrupt sale or as damaged by fire, emphasis is laid upon the distinction we make between restrictive laws and laws subjecting the individual to possible prohibition and executive control.

Chief Judge Cullen, at page 57, said:

"I concede that no vendor has a right to tell a falsehood as to his goods, be it material or immaterial, *and that the Legislature may properly pass laws to prevent or punish false statements.* The legislation before us does nothing of the kind. * * * *A vendor may own goods which have been purchased at a sale of a bankrupt or damaged by fire, and he has the unqualified right to sell them, and the unqualified right to tell the truth about them.* He cannot, under the exercise of the police power be prohibited from enjoying both these rights. 'The right to buy, sell, barter and exchange property is a necessary incident to its ownership, and subject to reasonable regulations is as much protected by this provision of the Constitution as is the ownership itself.' (*City of Carrollton* v. *Bazzette*, 159 Ill., 283.) * * *

"*the fact that some persons engaged in the same business are dishonest does not justify legislation prohibiting either directly or indirectly, the business* (*People ex rel. Tyroler* v. *Warden*, etc., 157 N. Y., 116; *Wright* v. *Hart*, 182 *id.*, 330).

"The counsel for the respondent relies largely on the authority of *People ex rel. Schwab* v. *Grant* (126 N. Y., 473), where it was held that to pursue the business of an auctioneer in the City and County of New York, a license was necessary, and that it was discretionary in the Mayor whether to grant or refuse a license. *It must be always remembered that law, even constitutional law, rests not wholly on principle, but in part on custom and tradition.* * * * Chief Judge Ruger, in the Schwab case, shows that during and ever since Colonial times, the calling of auctioneer had been regarded as a vocation *not open to all*, but subject to special license and authority" (italics ours).

See also *Chaddock* v. *Day*, 75 Mich., 527, holding unconstitutional an ordinance requiring a license for the sale of meat.

In *Lochner* v. *New York*, 198 U. S. 45, at p. 63, this Court cited with approval the State cases holding unconstitutional statutes regulating the trade of horseshoeing, including the case of *Bessette* v. *People*, 193 Ill., 334. In the latter case a distinction between a license fee for revenue and a license fee for regulation was clearly drawn. The Court said (p. 343):

> "Therefore, the proper construction of the act being that the license fee is imposed for regulation and not for revenue, the question arises whether the occupation of horseshoeing is such an occupation as the Legislature has any power to regulate in the manner provided for in this act."

After citing the case of *Powell* v. *Pennsylvania*, 127 U. S., 678, and *Allgeyer* v. *Louisiana*, 165 U. S., 578, the Illinois Supreme Court said (p. 345):

> "Although the power and discretion which the State Legislature has in the matter of promoting the general welfare, and of employing means to that end, are very large, yet such power must be so exercised as not to impair the fundamental rights of life, liberty and property. And although the Legislature may determine when the exigency exists for the exercise of the police power, yet it is for the Courts to determine what are the subjects of the exercise of this power."

Two especially well considered cases dealing with the regulation of the nursery business, and holding that the right to engage in it may not be subjected to discretionary license or bond, are

ex parte Hawley, 22 S. D., 23, 15 L. R. A. N. S., 138, and *In re* Schechter, 63 Fed., 695.

3. It is urged that "the prevention of fraud" is within the police power of the State. No one would question this general dictum. The Courts have also said that the police power extends to the promotion of the general welfare, comfort and convenience of the public.

Whatever confusion there may be as to the use of the term "police power," it is not, we think, apt to mislead the actual decision of the Court in any given case. There has been some criticism as to the broad use of this term in cases dealing with railroads and matters outside of the essential public needs. The point of course is that railroads fall within the general power of the State over public highways and over utilities exercising the right of eminent domain. The police power as such, in a very special sense, has been used to cover only those "great public needs" represented by the "public peace, health, morals and safety". The term has also been more broadly used as synonymous with governmental power, notably in cases dealing with the incidental injury, "*damnum absque injuria*," flowing from public improvements. In the early law this doctrine seems not to have been rested on the police power, but in later cases it is so classified.

> *Gilman* v. *Philadelphia*, 3 Wall, 713, 729;
> *Hamilton* v. *Vicksburg*, 119 U. S., 280;
> *C. B. & Q. R. R.* v. *State of Illinois*, 200 U. S., 561.

In these and similar cases the term is practically synonymous with the powers of government.

Mr. Justice Harlan, in *Lake Shore, etc., R. R.* v. *Ohio*, 173 U. S., 285, 297, intimates that this Court prefers the broader use of the term. Dealing with and referring to railroad legislation he said:

> "It may be that such legislation is not within the 'police power' of the State, as those words have been sometimes, although inaccurately, used. But in our opinion the power, whether called police, governmental or legislative, exists in each State, by appropriate enactments not forbidden by its own constitution or by the Constitution of the United States, to regulate the relative rights and duties of all persons and corporations within its jurisdiction, and therefore to provide for the public convenience and the public good."

It is plain from this *dictum* that the police power as so used is synonymous with governmental or legislative power as elsewhere used, and is not necessarily synonymous with the term as used in other cases dealing with the protection of the public peace, health and safety.

The use of the term in the different classes of cases by no means implies that legislation to promote the public convenience may authorize the executive to seize the person or property of the individual in the same way as is permitted to legislation relating to public health. Nor, we think, does it mean that legislation to prevent fraud in individual transactions of purchase and sale may take the form of subjecting the right to engage in such transactions to discretionary executive license, because the latter power is exercised over the milk business or over the banking business where fraud endangers the public health or destroys the safety which it is the special quasi-public function of a bank to pro-

vide for the imperative business needs of the community. No decision, we believe, can be cited in this or in any of the higher State courts, in support of such a view.

The power of prohibition against a particular commodity was asserted in *Powell* v. *Pennsylvania*, 127 U. S., 678, and the power of prohibition against a particular method of doing business was asserted in the recent case of *Rast* v. *Van Deman*, 250 U. S., 342.

In the former case the act was rested primarily on the protection of the public health, being entitled, "An Act for the protection of public health and to prevent adulteration of dairy products and fraud in the sale thereof." Mr. Justice Harlan, referring to the offer made in the Court below to prove that the particular articles sold by the defendant were wholesome, said (684):

> "It is entirely consistent with that offer that many, indeed, that most kinds of oleomargarine butter in the market contain ingredients that are or may become injurious to health. The Court cannot say, from anything of which it may take judicial cognizance, that such is not the fact. * * * Whether the manufacture of oleomargarine or imitation butter, of the kind described in the statute, is, or may be, conducted in such a way, or with such skill and secrecy, as to baffle ordinary inspection, or whether it involves such danger to the public health as to require, for the protection of the people, the entire suppression of the business, * * * are questions of fact and of public policy which belong to the legislative department to determine."

We believe that in all the later so-called "oleomargarine" cases, the statutes have simply pro-

hibited the sale of oleomargarine colored to resemble butter.

Plumley *v.* Massachusetts, 155 U. S., 461.

In *Rast* v. *Van Deman,* the whole conflict on the question of the interference with the liberty of a citizen centered upon the argument that the trading-stamp business was simply a normal method of advertising. The decision was rested on the view expressed by Mr. Justice McKenna as follows (p. 365):

> "The schemes of complainants have no such directness and effect. They rely upon something else than the article sold. They tempt by a promise of a value greater than that article and apparently not represented in its price, and it hence may be thought that thus by an appeal to cupidity lure to improvidence. This may not be called in an exact sense a 'lottery'; may not be called 'gaming'; it may, however, be considered as having the seduction and evil of such, and whether it has may be a matter of inquiry, a matter of inquiry and of judgment that it is finally within the power of the Legislature to make."

In the present case we are dealing with a prohibition not of a particular and novel method of doing business, a method conceivably pregnant with a special danger to the public, but with a prohibition of an entire business consisting primarily of a succession of normal individual transactions. The right is asserted, not to prohibit specific methods of carrying on this business nor of requiring specific safeguards against fraud, but of prohibiting the whole business, unless in the first instance the right to engage in it is granted

by an administrative officer or board upon its determination of the essentially administrative question as to the character of the individual.

Unless we start with the proposition that the right to sell securities owned by individuals as a business is not an inherent right, it is difficult to conceive of any other principle upon which such power may be upheld. The determination as to the character of the individual must be essentially an individual determination of the particular officer or board. It applies not alone against local dealers known in the community, but against dealers of other states and remote cities. Once such a question is held to be legally vested in an administrative officer, its exercise becomes potentially arbitrary beyond the power of real protection in the courts. We believe that to concede this point is to concede the power of complete control over a business which is essentially individual and competitive. Such a power once asserted and exercised is bound to destroy the normal interstate business in the sale of securities.

We repeat, therefore, that unless the power of complete prohibition exists, and unless the individual has no right to sell his property "in the course of continued or successive transactions of a similar nature," the Legislature cannot make the exercise of this right subject to the determination of an administrative officer or board.

4. There have been many attempted classifications of businesses "affected with a public interest" and subject to executive control.

Freund on Police Power says (Sec. 373):

> "Omitting those kinds of business which are subject to a special control in the interest of

peace, safety, health and morals, and which involve only the police power in the narrower sense of the term, the following have been classed from time to time as in a special sense public occupations or classes of business; at common law, the business of the carrier, innkeeper, ferryman, wharfinger, miller; the character (sic) is frequently indicated by the term public or common carrier, etc.; by modern statutes, and in addition to the common law, the business of railroads and the telegraph and telephone; also the management of turnpikes and canals; storage of grain and tobacco and the business of stock-yards; the supply of water, gas, light, heat, and power, through pipes and wires; banking and insurance; under recent judicial decisions also the gathering and distribution of news and market quotations."

Both the text-writers and the Courts have said that one class of business was subject to one kind of regulation, and another to another kind. This is of course true. The basis upon which the right of control rests is different in different classes of business, and the control asserted in the first instance is directed to one or more particular evils. Leaving aside, however, some of the smaller and exceptional classes of business and local nuisances subject to municipal regulation, and dealing with the important businesses which have been held subject to discretionary administrative control, such as the railroads, banks, insurance, and liquor business, it is, we believe, now true:

First. That they are subject to complete power of prohibition against the individual.

Second. That they may be confined to corporations.

Third. That they may be taken over and operated by state.

It is also true and important to note that each of them are susceptible to administrative control, and if necessary of complete ownership and operation by the State.

The prohibition in the present act against the business of buying and selling securities, is, we think, in principle that which has been asserted against the important business mentioned. The scheme of the present Act is similar in effect to that of an act prohibiting the business to the individual and requiring it to be done under corporate charter subject to conditions prescribed including subjection to executive control.

It is of value to quote in this connection from "Say's Political Economy, note to p. 134," as quoted in the opinion of the Court in Beebe *v.* State, 6 Ind., 505:

> "A government is guilty of an invasion upon the faculties of industry possessed by individuals, when it appropriates to itself a particular branch of industry * * * or when it sells the exclusive privilege of conducting it."

We have dealt with the licensing of the business on the assumption that its purpose is the prevention of fraud as a "great public need." The further "public need" of preventing loss through speculation becomes evident when we study the act in more detail under Point III.

(5.) The business of dealing in the stocks and bonds of corporations is not one "clothed with a public interest," and, therefore, subject "to be controlled by the public for the common good," within the principle laid down in *German Alli-*

ance Insurance Co. v. *Lewis,* 233 U. S., 389, and the cases upon which it was decided. In holding as this court did in that case, the business of insurance to be of such a character as to justify the State in fixing the rates and charges which might be made for services rendered by the business of fire insurance companies, the court pointed out that the decisions in *Munn* v. *Illinois,* 94 U. S., 113; Budd *v.* New York, 143 U. S., 517, and *Brass* v. *Stoeser,* 153 U. S., 391,

> "demonstrate that a business, by circumstances and its nature, may rise from private to be of public concern and be subject, in consequence, to governmental regulation" (p. 411).

and cited with approval the language of Judge Andrews in *People* v. *Budd,* 117 N. Y., 1, 27:

> "The underlying principle is that business of certain kinds holds such a peculiar relation to the public interests that there is superinduced upon it the right of public regulation."

The court then analyzed the business of insurance to determine whether or not it was within this principle. It adverted to the fact that from as early a period as 1837 the State has stepped in and imposed conditions upon insurance companies restraining the absolute liberty which businesses strictly private are permitted to exercise.

Now, the facts submitted in the present case show that there is no mature universal sense of the people regarding the regulation of the sales of stocks and bonds. The entire history of the leg-

islation began in Kansas in the year 1909. In five years it extended itself. It ran rapidly like a brush fire, and is not saved by any continued persistence "from the charge of unconsidered impulse." So far from having the characteristics of that universally widespread public belief which has found expression for nearly a century in the regulation of the business of insurance, it is shown to be sporadic, ill-considered and adventitious. It flared up suddenly under popular agitation and has died down as rapidly. An equally widespread clamor easily might be cultivated regarding the management of department stores, or of any of the other manifold activities of business life which the constitution and free institutions protect from the meddlesome interference of governmental bureaucracy. The reasoning of Judge F. C. Munger in holding a statute of Nebraska undertaking to fix the maximum rates and premiums that any fidelity or insurance company transacting business in that State might charge for furnishing bonds and undertakings is applicable here. See *American Surety Co.* v. *Shallenberger*, 183 Fed., 636. He there said (639):

> "The public interest in the business of such companies is no different in kind, from its interest in the business of any large mercantile or manufacturing company, whose capital, experience, and facilities may enable it to have widely extended patronage, but such characteristics do not make the business one which is affected with a public interest." Citing (*State* v. *Associated Press*, 159 Mo., 410.)
>
> "If the state may fix the amount of compensation for which an insurer may lawfully contract for furnishing such insurance, the state may dictate the price for which all other

> commodities shall be sold, including the price which may be paid for labor. This cannot be done. The fourteenth amendment to the Constitution protects the right of those engaged in purely private business to fix the price at which they will sell their services or commodities." (Citing Chesapeake & Potomac Tel. Co., 186 U. S., 238-246.)

The business of furnishing surety bonds is not a business of insurance within the general meaning of fire, life and marine insurance. True, in a certain sense surety bonds are contracts for indemnity against loss; but the obligation of the surety upon the bond is a guaranty for the personal performance of an assumed obligation. The obligation of the underwriter of a policy of life or fire insurance is an agreement of indemnity against impersonal loss, that is, loss caused by disaster for which no individual may be responsible; against the contingency of accident or death. The business of furnishing corporate suretyship in lieu of individual guarantors is of recent growth, and has no such record of long-continued public regulation as to "exhibit it to be the conception of the law-making bodies of the country without exception that the business of (that kind of) insurance so far affects the public welfare as to invoke and require governmental regulation" (233 U. S., 412).

Judge Pollock, in writing the decision of the lower court in *German Alliance Insurance Co.* v. *Barnes*, 189 Fed., 769, 778, cited, in support of the proposition that the business of fire insurance, although in its nature a private business, was affected with a public interest, quoted from the opinion of Mr. Justice Harlan in *German Alliance Insurance Co.* v. *Hale*, 219 U. S., 307, wherein was involved the constitutional validity of an act of the State of

Alabama, which provided for the recovery by the assured from the company of 25% more than the actual loss sustained, on a mere showing that the company writing the contract belonged to the Insurance Tariff or Rate Association, wherein he said:

> "We concur entirely in the opinion expressed by the state court that the statute does not infringe the Federal Constitution, nor deprive the insurance company of any rights granted or secured by that instrument. The business of fire insurance is, as every one knows, of an extensive and peculiar character, and its management concerns a very large number of people, particularly those who own property and desire to protect themselves by insurance. We can well understand that fire insurance companies acting together, may have owners of property practically at their mercy in the matter of rates, and may have it in their power to deprive the public generally of the advantages flowing from competition between rival organizations engaged in the business of fire insurance. In order to meet the evils of such combinations or associations, the state is competent to adopt appropriate regulations that will tend to substitute competition in the place of combination or monopoly * * *" (p. 316).

And he held that the principle underlying the enactment in that case and the case then before the court was the same.

Counsel for the State of Kansas in the *German Alliance Insurance Co.* case, after a review of the history of governmental regulation of fire insurance business and the scope of the statutes enacted in pursuance of such regulation, argued in the Supreme Court that said enactments

> "are conceded to be within the power of the state, not alone because these companies are corporations, but because they are engaged in the business which affects the public at large on account of its magnitude and on account of the fact that it is so centralized, within the control of certain large corporations the management of whose business is so intricate that the average private citizen in dealing with them is placed entirely at a disadvantage, and which makes it easy for the companies themselves by private agreement to entirely and arbitrarily regulate and control affairs which are of great importance to every citizen in this state" (Brief, p, 9).

This argument was also employed by Justice McKenna in delivering the opinion of the Court (233 U. S., 414-416).

Such facts have no application to the case at bar. There is no centralized control over the business of selling securities and no state of affairs which makes it easy "for the companies themselves by private agreement to entirely and arbitrarily regulate and control affairs which are of great importance to every citizen in the State." There is nothing respecting the business of buying and selling securities substantially different from other kinds of commercial business. There are of course opportunities for fraud in this, as in every business. There is the temptation of cupidity on the side of both the purchaser and seller, and the same contingencies of gain or loss, anl unless we are to substitute the paternal government of the Socialists for the Constitutional liberty of our ancestors, such statutes as the Blue Sky Legislation of Michigan, Ohio, and other States, of similar character must fail.

POINT III.

One who "in the course of continued or successive transactions of a similar nature" offers or sells securities owned by him, cannot be prohibited from making a particular offering or sale except upon a "certificate of authority" from a State Commission.

1. For the purposes of this appeal, these appellees are not inclined to stress any particular construction of Section 9. The purpose both of the 1913 and 1915 Act, as of the 1911 Kansas Act, is to reach something less definite and more broad than provable fraud.

It is evident from the careful wording of the act, and from its repetition, that its prohibition is intended to apply even though the act might not be found in fact fraudulent—fraud requires intent and a *finding* requires evidence to support it. The transaction is prohibited if its effect would be *to work a fraud in the opinion of the administrative board.* The most limited sense that can be given to this clause seems to us to be, that, even though a fraudulent intent cannot justly be ascribed to the promoters, yet if in the opinion of the Commission he has deceived himself and is deceiving others as to the merits and prospects of his scheme, which is in its opinion unsafe and will probably prove disastrous, then it would in its opinion "work a fraud on the purchaser," deceive him and cause him loss. This deception and this loss, though unintended, the Act plans to prevent by its prohibition based on the disapproval of the Commission.

This idea is the crux of the Act, its purpose be-

ing to prevent something more than provable fraud.

Such was the purpose of the original Kansas Act and it survives in this Act. The investor is to be protected against his own gullibility, against the wiles of a John Law or Harley; against the visionary hopes of a Stephenson, Fulton, Morse, Bell, Whitney, Ford, Marconi, Holland or Wright.

The genius and enterprise of the future is, if possible, to be tied to the wheel of a government bureaucracy in each of the fifty States. This bureaucracy must have a depth of insight and expert knowledge sufficient to detect the latent fraud by which, as the Attorney General of Iowa has said, the "well-informed business man" is often deceived. If it fails, it gives to the fraud the sanction of the State and entails more loss to the very class sought to be protected, the class ignorant enough to rely on its protection, than it can possibly prevent by its restriction. This bureaucracy must on the other hand have a breadth of vision and expert knowledge sufficient to see the untold wealth pregnant in a new invention. If it fails, if it finds that the sale of securities based on a vision of promised value would work a fraud on the gullible purchaser, if it refuses under Section 8 to sanction the issue of $100,000 in stock for an invention worth in fact $100,000,000, the vision and the invention may die aborning.

Need we ask the Court to take judicial notice of the fact that this superhuman perfection, this deep insight, broad vision and expert knowledge covering all the fields of human endeavor, does not ordinarily reside in the Bank Superintendent or the State Treasurer or even in the Attorney Gen-

eral of any of the several sovereign states of the American Union?

Is it not clear, that when by the publicity feature of the acts, we have driven away the obvious frauds, the act, Section 9, becomes in its necessary effect an evil incalculably greater than any other evil remaining to be remedied?

Birth-control cannot be substituted for the demonstrated events of life.

Consider for a moment the variety of enterprises upon which the Commission must pass—a commercial business in Michigan, a railroad in China, a gas or power utility in California, a timber enterprise in Panama or British Columbia, an asphalt property in South America, and an invention to revolutionize the automobile industry.

As to none of these in fact does the state undertake to supply an expert judgment. It desires to substitute for the judgment of a poor widow or uninformed farmer the judgment of a lay political official or employee. But if it decides that the proposed sale to such an investor would work a fraud on him, its prohibition prevents the most wide-a-wake business man from purchasing securities in the full exercise of his own judgment. If having in mind the wide-a-wake business man, it applies the act liberally, it opens the door to greater loss to the poor investor.

The purpose is to protect a minority of "investors," looking for vast gains, against a danger existing in a small minority of transactions. To accomplish this it prohibits all investors from buying securities without the approval of the Commission.

2. *The law is primarily prohibitive.* It prohibits the act absolutely in the first instance, and then authorizes an application to the Commission for authority to do it.

It does not prohibit particular wrongs, but it prohibits an entire business and each of a multiplicity of transactions connected with it, unless (1) the business and (2) each of such transactions is officially approved and permitted.

We have mentioned the fact that businesses such as those of railroad and banking may be denied to the individual and limited to corporations chartered by the state, doing business as conditioned in their charters. In practical effect that is what is here done. The transaction is (1) prohibited and (2) permitted in a special way under the license and control of a State Board.

The law (except the final provision in section 3, *infra*) does not authorize an investigation of particular cases and a finding by the Commission of the fact or conclusion of fraud or deception, and then prohibit only the thing found to be fraudulent. It prohibits a hundred transactions, because, one of them may be fraudulent, and compels the ninty-nine innocent parties to get a permit and pay a fee, and to establish their honesty and the sound basis of their proposition before they can sell a share of stock.

This prohibition is in fact final as to a very large proportion of the transactions covered by it, including the normal business involved in the sale of one to ten or twenty bonds to a particular investor. It in actual effect confines offerings to a few flotations having a profit to the promoter or dealer sufficient to justify the burden and expense imposed.

Where not completely prohibitive in the first instance, it will become completely prohibitive as to any normal offering of investment securities the moment the Commission exercises its uncontrolled discretion of conducting an extended investigation of the property and business at the expense of the applicant. Argument and instances are hardly necessary to support this statement. A normal offering of investment securities would not stand this unlimited expense in one state, let alone in the four to twenty in which otherwise it would be made. This power is practically uncontrolled.

3. Legal Character of Control. The power given to the Commission is in form that of determining the character of particular transactions, first, to "find" that it is "fraudulent;" second, to "find" that in its own "opinion" it would 'work a fraud" on the purchaser.

The power given to the Commission is in substance that of complete governmental control, (1) over the prevention of fraud in the issuance or sale of securities, with a duty to prevent fraud and (2) over the prevention of loss through mistakes as to fact in the purchase of securities with a duty to prevent loss.

It is the substance, rather than the form, which concerns us on this appeal.

Dealing with the form in which the Act presents the question, the invalid feature of the Act is the initial prohibition. If this were valid, if all transactions might be prohibited, there could be no objection to the grant of permission upon the finding of an administrative board as to a particular transaction. Such a power, within its

proper field, is administrative in character, though both quasi-judicial and quasi-legislative in its operation and effect.

It cannot be said that the powers given the Commission are *in form* legislative. The Legislature may issue licenses and grant charters of authority, but it can also authorize an executive to do it. In either case, there is no occasion for a license or authority unless either (1) the thing granted is something in its nature beyond individual right, or (2) can be properly denied to individuals and converted into a privilege to be granted by the State.

Nor are these powers *in form* necessarily judicial. There is no legal adjudication of particular right or wrongs, simply a determination of judgment in the exercise of discretion, as a basis for prohibiting or permitting a thing to be done.

Dealing with the substance, we have a delegation of complete power, including the legislative and the judicial, over an entire field of governmental action, a field of ordinary legislation, a field in which it is the essential function of the Legislature to declare the law, and of the Courts to adjudicate particular rights and wrongs under it.

The question comes back finally to one of prohibition. If the act may be prohibited, it may be made a matter of administrative license; if it may not be prohibited, it may not be made a matter of license.

We repeat that the thing prohibited is not fraud. It is the transaction. It is made a matter of license, instead of a matter of right without a license. A whole field of ordinary legislation is abandoned to the actual government and con-

trol of an administrative commission. This field is the prevention of fraud or improvidence in the sale or purchase of securities.

4. The prohibition of the right to buy and sell, its conversion into a privilege subject to executive permit, deprives the person both of liberty and property without due process of law. It is not within the Police Power.

> "The liberty of the citizen includes the right to acquire property, to own and use it, to buy and sell it. It is a necessary incident to the ownership of property that the owner shall have the right to sell or barter, and this right is protected by the constitution as such an incident to ownership. When an owner is deprived of the right to expose for sale and sell his property he is deprived of property."
>
> *Chicago* v. *Netcher*, 183 Ill., 104, 110.

See also:

> *State* v. *Indiana Oil Co.*, 120 Ind., 575, 583.

> "The legislature may properly pass laws to prevent or punish false statements. The legislation before us does nothing of the kind * * * A vendor may own goods which have been purchased at a sale of a bankrupt or damaged by fire, and he has the unqualified right to sell them, and the unqualified right to tell the truth about them * * * the fact that some persons engaged in the same business are dishonest does not justify legislation prohibiting, either directly or indirectly its business."
>
> Chief Judge Cullen in *People* v. *Jenkins*, 202 N. Y., 53, at p. 57.

Much that has been said under Point II with reference to the prohibition of the business applies with even greater force to the prohibition of the individual transaction.

The fact that the police power may permit the destruction of a building endangering public safety, or the seizure of an infected individual or an infected cow endangering public health, does not mean that it permits the confiscation of the right to sell property because, in the opinion of the executive board, its purchase would work a fraud on one or more possible individual purchasers.

The fact that the State which creates a railroad, may by executive act fix or limit its rate of charge, does not mean that it may by like act condition or control the right of bargain and sale.

"The police power extends to the great public needs." (Mr. Justice Holmes in the Oklahoma Bank case.)

"But necessarily it has its limits and must stop when it encounters the prohibitions of the Constitution" (Mr. Justice McKenna in Eubank *v.* Richmond, 226 U. S., 137).

What is the great public need on which this legislation is founded? The evil which it is the purpose of the present act to remedy is stated in the appellant's brief to lie in the sale of "fraudulent mining stocks, oil stocks and other fly-by-night ventures."

We have seen that the so-called "fly-by-night," or "get-rich-quick," or "blue-sky" dealings do not constitute more than one per cent. at the outside of the total dealings in securities. We have seen that as to the normal business there has been no

charge that fraud is prevalent in the distribution of securities.

It is also to be emphasized that this so-called dangerous class of securities is fairly well earmarked and could at least approximately be defined and reached by legislation requiring adequate safeguards against its special dangers.

It is said that the supervision of banks rests on the need of preventing fraud and loss to the community, and that therefore the prevention of fraud as such justifies executive control. The answer is plain. The savings of a whole community are in the bank or banks of the community. The bank invites its depositors to create a common fund and itself performs a quasi-public service to the community in receiving deposits subject to check, as well as in caring for and investing the savings of the community. Fraud or waste in the management of the bank involves not only a loss but may well involve a community bankruptcy or a national panic.

It might be argued that in rare instances fraudulent flotations have been so widely distributed that the losses have fallen on a whole community. Yet, in fact, even in the extreme cases, this is never so. The investments are essentially individual, and the fraud, if practiced, is individual. The losses sustained by fraud, as distinguished from losses due to wide-spread depressions and panics, are individual. The evil in its essence is simply an important one of the many individual wrongs which should be the subject of effective remedial legislation.

The following dictum of Mr. Justice Wheeler, sitting in Special Term of the Supreme Court of New York, is apt:

> "The statute is not addressed to the punishment of fraud where actually committed, but is rather a prohibition against certain acts for fear fraud may be perpetrated. *The legislature might with equal propriety and upon the same argument pass an act prohibiting certain persons trading within the state in order that they might not possibly perpetrate frauds upon those with whom they deal.* * * * It is not legitimate legislation to prohibit the prosecution of a lawful business or calling because some unscrupulous person may in connection with it perpetrate a fraud. The thing to do is to prohibit and punish the fraud—not the business."
>
> People *v.* Vandell, 146 N. Y. Supp., 992, 994.

What we have said applies to fraud as a basis of a public need within the field where it prevails. This was the great public need visioned by Mr. Dolley in his original "blue-sky" agitation. Close upon it followed the purely bureaucratic idea of giving "valuable advice" to the public, to be "of much assistance to them in investing money where it will not be lost." A year later it had come to pass that "the law is rapidly gaining fame all over the civilized world. I believe that a movement has been started that will eventually result in the regulation and supervision of all kinds of companies in the same manner as banks are now regulated by law."

Here is a new public need. Is it in the opinion of this Court a "great public need"?

The following quotations are taken from Dr. William Bondy's excellent discussion entitled "The Separation of Governmental Powers," published by Columbia College in 1896.

MONTESQUIEU:

"When the legislative and executive powers are united in the same person or body, there can be no liberty." (p. 13, 14.)

WASHINGTON:

"The spirit of encroachment tends to consolidate the powers of all departments in one, and thus to create, whatever the form of government, a real despotism."

MADISON:

"The accumulation of all powers, legislative, executive and judicial in the same hands, may justly be pronounced the very definition of tyranny."

JEFFERSON:

"The concentrating these in the same hands is precisely the definition of despotic government."

ADAMS:

"It is by balancing each of these three powers against the other two that the efforts in human nature toward tyranny can alone be checked and restrained and any degree of freedom preserved."

HAMILTON:

"I agree that there is no liberty if the power of judging be not separated from the legislative and executive powers." (p. 17.)

WEBSTER:

"* * * doubtless the continuance of regulated liberty depends on maintaining these boundaries." (p. 18.)

BLACKSTONE:

"Were it (the judicial power) joined with the legislative, the life, liberty and property of the subject would be in the hands of arbitrary judges whose decisions would be regulated only by their *opinions, and not by any fundamental principles of law*, which though legislators may depart from, yet judges are bound to observe." (p. 14; italics ours.)

5. The scheme of the Act is attempted to be upheld on the principle that the "Legislature can make a law to delegate a power to determine some fact or state of things upon which the law makes or intends to make its own action depend." To deny this would be to stop the wheels of government" (Locke's Appeal, 72 Penn., 491, 498). But see

Willoughby on the Constitution, Section 776.

Cooley, Constitutional Lim., 7th Ed., page 163.

To the objection "made in the Court below that no fixed standard for the guidance of the Commission was found in the law" our adversary exclaims (Appellants' Brief, p. 25):

> "How absolutely impossible such a thing would be must be apparent, and how readily the law could be evaded if a fixed standard was present in the Act goes without saying."

The same comment would hold if the same principle were applied to any other field of legislation.

Let the Legislature prohibit any and all schemes, transactions, or parts thereof, which in the opinion of the Governor would tend to defraud or to cause improvidence or loss, or to encourage gambling or immorality. Then upon the determination of the Governor that a particular act or thing being done or contemplated by John Jones to or with Tom Smith or Mary Brown was within one or another of the things mentioned, let him

sign a finding and send it to John Jones, thereby prohibiting him, *i. e.*, John Jones, from doing that particular thing.

Can it be said that the law-making power is vested in the Governor? Perish the thought! He simply "determines some fact or state of things upon which the law makes or intends to make its own action depend." To deny this would be to stop the wheels of government."

So far as lies within our power on this appeal, we profess a desire to "stop the wheels of government" at or about this point. They have as yet gone not too far, nor perhaps far enough, but if they ever attempt to go by administrative process over individual transactions and private business, they will, we think, have ceased to be "the wheels of government" and become the hoofs of an autocrat.

We have already pointed out what seems to us to be the potentially complete character of administrative control over quasi-public businesses and matters of public right. The tendency of modern decisions is, we believe, to re-assert, rather than to create, the full power necessary to their effective control, and to recognize the fact that control of one of its interrelated parts means, in the last analysis, the power of complete control.

There are also, of course, other subjects of prohibition and administrative control, distinct from any business, such as the control over the use of streets and public places, and the far-reaching control necessary at times for the protection of the public health, peace and safety, to which may be added the control over foreign commerce and over aliens which has been vested in the President, and the control given various officials or boards over

governmental agencies, such as the post office, and governmental property, including public parks and reservations.

It is, we think, indisputable, that as to each and all of these businesses and subjects, the control vested in the administrator rests solely on the original principle or necessity on which it was first asserted, that it is historically and constitutionally an administrative power, the vesting and conditions of which are subject to law, that is to legislative grant and control.

Such control not being legislative in its nature, an act vesting it in an administrator is in no sense a delegation of legislative power. Manifestly the Legislature may grant or withhold it, limit or condition it as it sees fit, and by the very nature of the case may, if it chooses, prescribe by law the details, the standards or the rules, to be followed by the Administrator.

Whether the whole matter be vested in the Administrator, or prescribed by the Legislature, the act of each is an act of the State, and is subject to the constitutional inhibitions against the impairment of contracts or the deprivation of property rights. There is no liberty, no liberty that is to engage in the railroad business, the banking business, the insurance business or the liquor business.

The question in each case is one of the exercise of the power within the constitutional inhibitions and, if by the Administrator, within the statute governing it, and in no way a question of the delegation by the Legislature of its essentially legislative power.

In the great majority of the cases dealing with this power, notably *Liebermann* v. *Van de Carr*, *Gundling* v. *Chicago*, *Engel* v. *O'Malley*, and the

German Alliance Insurance case, no question seems to have been raised as to the delegation of power. In a few cases, however, involving the same administrative control of a quasi-public business or of other matters clearly subject to such control, counsel, and at times Courts, have given weight to the argument that such control vested in the Executive was in some way touched by the constitutional rule or express prohibition against the delegation of legislative power, and have formulated principles relative to the delegation of legislative power, which, whatever bearing they may have in such cases, have, we submit, none in cases of ordinary remedial legislation.

In fact, it seems to be in precisely, if not exclusively, in such cases that there have been established what are quite generally recognized as the priinciples governing the delegation of legislative power.

Locke's Appeal, 72 Pa., 491.

in which the question was as to the licensing of saloons, a local option law.

Field v. *Clark*, 143 U. S., 649,

in which the question was as to the vesting in the President of the right to suspend a reciprocal tariff provision.

Buttfield v. *Stranahan*, 192 U. S., 470.

in which the question was as to vesting the Secretary of the Treasury, acting on the recommendation of an expert board, with power to fix a standard of purity for imported teas.

Union Bridge Co. v. *U. S.*, 204 U. S., 364,

in which the question was as to vesting the Secretary of War with power to cause the removal of a bridge as an unsafe obstruction to a navigable stream, *i. e.*, a public highway.

U. S. v. *Grimaud*, 220 U. S., 506,

in which the question was as to the construction of the power given the Secretary of Agriculture over a government reservation, and the validity of a regulation prohibiting sheep raising within a prescribed area.

I. C. C. v. *Goodrich Transit Co.*, 224 U. S., 194,

in which the question was as to the construction of the power given the Interstate Commerce Commission to require accounts of common carriers to be kept in a specified manner.

These cases sufficiently emphasize the point that in all instances where an actual discretionary power, or even the power to "determine some fact or state of things on which the law makes or intends to make, its own action depend," has been upheld, the Court has been dealing with a power historically and constitutionally administrative. This power is in nature a discretionary power. Instance the early statutes cited in *Field* v. *Clark* (pp. 683 to 692). Its rules and orders in the given field have all the force of law and are the law operating through a valid executive discretion upon the subject matter to which they relate.

Congress has the power to regulate commerce, but it is a power which must be exercised according to the character of the subject, and construed according to preexisting principles and

precedents applicable to the subject. These principles and precedents make it clear that the common carrier of commerce and the highways of commerce are to be controlled by an administrative officer or Board under laws to be adopted for that purpose. There is, we believe, no delegation of legislative power in vesting in such an officer or Board the broad discretionary powers historically and constitutionally proper for the purpose in view.

A law providing in terms that every interstate carrier should be licensed by the Interstate Commerce Commission and be subject in all respect to the conditions prescribed in such license, would, we assume, be free from constitutional objection.

A comparison of the *Yick Wo* case with the cases of *Lieberman* v. *Van De Carr* and *Engel* v. *O'Malley*, will, we think, bring out quite clearly the fact that this Court has concluded that the control vested in such cases may be discretionary in terms and is not affected by the principle of the delegation of legislative power. In the *Yick Wo* case Mr. Justice Matthews refused to accept the view of the Supreme Court of California that the ordinance then in question gave executive discretion "to be exercised with reference to the circumstances of the case, with a view to the protection of the public against the dangers of fire. We are not able to concur in that interpretation * * * they * * * confer a naked and arbitrary power * * * not only as to place, but as to persons." The Court also cited the case of *Baltimore* v. *Radecke*, 49 Maryland, 217, in which a similar view was taken of an ordinance under which the Mayor was authorized in general terms to revoke permits for the use of steam engines. Mr. Justice Matthews

instanced as proper legislation "that giving discretion * * * to grant or withhold licenses for taverns * * * one of the conditions is that the applicant shall be a fit person," emphasizing the need of some legislative guide or standard. In the *Gundling* case, the condition instanced by Mr. Justice Matthews was met, as the executive was required to be satisfied as to the good character of the person seeking the permit dealing in securities. In *Lieberman* v. *Van De Carr*, however, the Court entirely discarded the idea that the power delegated must be accompanied by any standard. Numerous cases were cited and the principle was unmistakably announced that the discretion given might be general and unqualified in terms. The same principle was applied with equal force in *Engel* v. *O'Malley*, to the business of banking.

Field v. *Clark*, and the various statutes cited in it (pp. 683 to 692) seem to us to rest chiefly and with unquestioned soundness on the necessity at times of vesting in the executive the complete power to deal with anything that affects our foreign affairs, to lay an embargo on foreign ships, to make or unmake restrictions applicable to our foreign commerce with all or with one nation, and to cite the most recent instance, to refuse clearance to vessels discriminating against American exports.

It is both interesting and pertinent to note that Mr. Justice Harlan emphasized the fact that "nothing involving the expediency or the just operation of such legislation was left to the determination of the President," and yet in the early statutes cited with apparent approval, practically uncontrolled discretion was given to

the President, necessarily, wisely and constitutionally. Though no historic review of the subject is at hand, it will hardly be questioned that here also we are dealing with a power which from time immemorial had been accustomed to be vested in the chief executive.

The same considerations apply with equal force to the cases upholding the exercise of executive power in the exclusion of aliens.

Fong Yue Ting v. *U. S.*, 149 U. S., 698.

A case close in character, but perhaps having an additional ground of support, is that of *Buttfield* v. *Stranahan*, 192 U. S., 470, upholding the Act of March 2, 1897, authorizing the Secretary of Treasury, upon the advice of an expert board, to prescribe standards of purity of teas imported into the United States. Can anyone question that if Congress is to legislate to safeguard foreign commerce in the interest of the public health, it must use the same executive expert instrumentalities which are available to a village board? In all these cases, though we think and speak of a delegation of legislative power, it is a vesting of administrative power not within or intended to be within either the letter or spirit of the constitutional rule of prohibition against the delegation of such power. We are dealing with matters properly within administrative control, and the reasoning and dicta by which the acts are upheld, have no relation to the questions of whether or not there is in fact a delegation in cases within the constitutional rule.

So, also, in *Union Bridge Co.* v. *U. S.*, *supra*, upholding Section 18 of the River and Harbor Act of 1899 (see opinion, page 386), the power to keep

open the navigable streams of a nation is no different in character from the power to remove obstructions in any public highway. It is a public duty that demands the exercise of administrative control that from time immemorial has been so exercised.

A decision somewhat out of the beaten track is that of *Public Clearing House* v. *Coyne,* 194 U. S., 497, in which this Court, Justice Peckham dissenting, upheld Section 3929 of the Revised Statutes authorizing the Postmaster General "upon evidence satisfactory to him," to exclude letters in aid of a lottery or fraud from the mails. The Court, page 506, by Mr. Justice Brown, pointed out that the transmission of letters had in times past been by private parties, and that the postal service

> "is not however a necessary part of the civil government in the same sense in which the protection of life, liberty and property, the defense of the government against insurrection and foreign invasion and the administration of public justice are; but it is a public function assumed and established by Congress for the general welfare and in most countries its expenses are paid solely by the persons making use of its facilities. * * * The legislative body in thus establishing a postal service may annex such conditions to it as it chooses."

In the alien cases, particularly in

> Ekiu *v.* U. S., 142 U. S., 65, citing U. S. *v.* Jung Ah Lung, 124 U. S., 621.

the Court made it clear that though the Legislature had provided for a hearing by the Courts to determine the facts, yet "on the other hand the

determination of those facts may be intrusted by Congress to the executive," with the power to exclude or deport the alien.

There are also many cases upholding the vesting of administrative power over matters essential to public health or safety, including the erection and removal of buildings, or affecting the use of the streets or public places. It is hardly necessary to discuss these cases, as they have been generally recognized, at least by this Court, as raising no question as to the delegation of legislative power.

There can be no delegation of a Legislative power unless the power is *essentially* Legislative. If the power in its nature is administrative, it is vested in the administrator by the Legislature, not delegated by the Legislature to the administrator; and this entirely irrespective of the fact that the Legislature as the law-making body might itself use its own judgment, determine the fact and apply the law. We are speaking of the discretion which may be given an administrator over public business, over foreign commerce, over Government lands and similar subjects. This discretion is not essentially legislative. It is not delegated but vested in the administrator; and this irrespective of the fact that the Legislature as the supreme law-making power might itself exercise all or part of the discretion and leave little or none of it to the administrator.

It is necessary to the efficiency of this control as applied in the large field subject to it, that it be liberally construed and potentially complete, leaving it to the Legislature to determine its bounds and conditions, to the Courts to keep it within the

bounds set by the Legislature and also within the bounds set by the constitutional inhibitions against the deprivation of property and the impairment of contracts.

This broad power cannot exist, it cannot be judicially recognized as it has been recognized, if the principle and precedents on which it rests are to be held applicable to the entire field of remedial legislation.

Locke's Appeal, 72 Pa., 491, the source of the oft-quoted dictum, illustrates very strikingly the inherent difficulties with which the Courts have had to contend. The majority opinion by Justice Agnew, one of the ablest jurists of a great bench, attempts with dubious success to distinguish and escape from the logic of Justice Bell's opinion in *Parker* v. *Commonwealth*, 6 Barr, 507, and Justice Sharswood replies to him from the bench with unanswerable force, making clear our present contention that the principle then announced as a general rule could never in any event be applied to matters of ordinary legislation (508).

> "There are a good many acts of executive administration which they can delegate to the Courts, or to the municipal corporations, or to the people of the different districts. But a 'law,' properly speaking, is a rule of conduct prescribed by the supreme power of the State, commanding what is right and prohibiting what is wrong.
>
> "*Now I think no one would doubt, if the legislature were to submit to the people of a county, or township, or ward, the question whether murder should be punished by imprisonment only, and let the people vote 'capital punishment' or 'no capital punishment,' that would be a law, and the legislature could not delegate it to the people.*"

On the premises assumed by Justice Agnew, he could not meet the logic of Justice Bell and was entirely refuted by Justice Sharswood. The weight of opinion now makes the question of "license" or "no license" one "of executive administration" which, as Justice Sharswood said, "they can delegate to the Courts or to the municipal corporations, or to the people of the different districts." That indeed was the ground first and soundly stated by Justice Agnew, when he said page 498, "what is the difference, in essence, whether the necessity for places for the sale of liquors be determined by the people or by the Courts." It was a local administrative question upon which it was proper for the Legislature to require the sense of the electorate. There was no delegation of legislative power, but only a submission to the electors of a matter of local policy.

Chief Justice Read also dissented in an able opinion. He took occasion also to refer to the proposed "centennial celebration to which we have invited the whole country," page 507:

> "On the 4th of July, 1776, every patriot drank to the independence of the thirteen states; shall it be that on the 4th of July, 1876, all we can lawfully offer to our guests on this great anniversary, will be a glass of Schuykill water, seasoned with a lump of Knickerbocker ice?

POINT IV.

The so-called standard manual feature of the act is unconstitutional and void.

It is evident that the Act with its sweeping prohibitions over an entire business would never have been adopted, or if adopted enforced, but for the subterfuge of the so-called manual exemption. The character of these manuals we have already discussed. It should, perhaps, be further stated that the really standard manuals such as Moody's and Poor's do not in fact "list" securities. They list the various corporations and publish various information as to each of them, including the amounts of securities issued.

The exemption intended to be effected is not merely an exemption of the securities of existing companies "listed" in the existing manuals established and used by financial houses. It is intended to cover, and does cover, securities hereafter listed in any manual hereafter approved by the Commission. *It is to be a permanent means of exempting new securities from the Act.*

The Commission is given a sweeping power to exempt securities in bulk; this regardless of any criterion whatever, unless the word "standard" is held to impose some indefinite limitation upon the manuals to be approved.

The approval by the Commission of a standard manual of information carries with it to the publishers of the manual the power to list additional securities, and by such listing to grant exemption from the Act. Different manuals are published at different periods and are, we believe, supplemented from time to time and *kept up to date.*

The affidavit of appellants (Record, p. 97)

states the character of the manuals which the Commission have approved, and that such manuals are standard manuals and "are such manuals as are in use by the bankers and investment public of the State of Michigan." This may be accepted as evidence of what they have done under the Act, but it does not have anything to do with the question as to the actual power given them. It is expressly charged in the complaint (Record, p. 11) that one of the manuals approved supplies "information as to failing concerns and as to fraudulent securities as matters of information to their clients." There is nothing in the Act inconsistent with the approval of such a manual.

It need, we think, hardly be argued that this power of sweeping exemption from the Act is left to the practically uncontrolled discretion of the Commission. It constitutes a complete delegation of legislative power to the Commission and also deprives appellees owning securities not listed in the approved manuals of the equal protection of the laws. There is no basis whatever for the classification except the assumption, contrary to the fact, that fraudulent or "get-rich-quick" securities would not in any event be listed in a manual approved by the Commission.

It should also be noted that the listing in the manual carries with it not only exemption from the need of securing an executive permit, but also that it carries with it absolute and complete exemption from the prohibition of Section 8 against the sales of securities issued for property in excess of its value. Many such securities are of course listed in these manuals.

2. The *proviso* to this exemption presents a separate and important constitutional question.

Bearing in mind that the vast majority of securities which would otherwise be within the primary prohibition of the Act are in fact listed in the manuals, it follows that the proviso to the exemption constitutes the actual working law as applied to the majority of outstanding securities, as well as to a very large part of new securities issued

There is, here, no absolute prohibition of all offerings, but power in the Commission to

> "call for additional and further information than that contained in such manuals with reference to any securities listed therein, and * * * pending the filing of such information suspend the sale of such securities, and also *suspend temporarily or permanently, the sale of any securities listed in such manuals after a hearing upon notice to the issuer* * * * *if such Commission shall find* * * * *that the sale* * * * *would work a fraud upon the purchasers thereof.*"

Ignoring the unworkable character of this proviso, and the fact that under it the right to sell securities might be suspended without any notice whatever to the actual owners thereof, we have as a substantial proposition the vesting in the Commission of the power at any time to prohibit the sale of particular securities upon its finding as stated.

As to these securities the Act makes no prohibition. They are not in the first instance subject to the law. They are, however, made conditionally subject to the new law-making power of the Commission; that is, to its power to prevent their future sale by administrative mandate at any time. There is no prohibition until the mandate issues, and from that time forward there is a prohibition.

It seems to us quite clear that this is a specific law-making power vested in the Commission over a vast subject-matter of private business and individual transactions.

Here, also, it is urged that the Commission is simply vested with the power to "determine the fact" upon which the law operates. The "fact" to be determined is plainly a conclusion based on "information" contained in the manuals and obtained from unknown sources as to whether or not the sale of such securities comes within a broad legislative field, the control of which is given to the Commission.

Here we have specifically the instance assumed under Point III. The Legislature instead of adopting a law, a rule of conduct prescribing what is right and prohibiting what is wrong, attempts to delegate to the Commission the complete power covering a given field both to determine what is wrong and to prohibit it, to "suspend * * * permanently, the sale of any securities * * * if said Commission shall find that the sale * * * would work a fraud."

The invalidity of the proviso as such destroys the whole Act. Without it it is evident that the exemption would not have been made, and without the exemption it is evident that the Act would not have been adopted.

POINT V.

"The regulations are so utterly unreasonable and extravagant in their language and purpose that the property and personal rights of a citizen are unnecessarily and in a manner wholly arbitrary, interfered with and destroyed without due process of law."

Gundling v. *Chicago,* 177 U. S., 183, p. 188.

1. Little remains to be said on this specific point. We call attention to the fact that the Act goes far beyond the original purpose of the Blue Sky legislation; that it prohibits the entire business and a multiplicity of individual transactions, in order to reach a limited and special class of transactions which are essentially outside of the normal business. On the assumption that one man in a hundred contemplating fraud, the whole hundred are subjected to prohibitions which, as to a large number of perfectly innocent transactions, is necessarily completely prohibitive.

2. The prohibitions of Section 8 are utterly unreasonable and unnecessary for any proper purpose. While to prevent the issue of securities for property at a nominal valuation in excess of real valuation, is undoubtedly within the power and duty of the State creating the corporation, yet after that State has in fact authorized and permitted the issuance of such stock, presumably full paid according to its laws, the stock when issued is an undoubtedly property right, and there is no presumption of fraud or wrong of any kind in its attempted sale.

The duty of fixing the value of property for which stock is issued is in most States vested in the

corporate officers; in some States it is vested in state officials. The presumption must, we think, be that there has been in all cases a valid determination of this fact and that in the judgment of competent authorities the stock has in fact been issued for full value. Notwithstanding this presumption, Section 8 entirely prohibits the sale of the stock in Michigan if upon investigation the Michigan Securities Commission disagrees with the value which has been placed upon the property by the authorities of the issuing State. It is to be noted that this prohibition is absolute as against all non-exempt securities and would apply to securities outstanding for many years. A dealer cannot sell them within the state.

(3) The power given the Commission to "make or have made under its direction a detailed examination of such investment companies' property, business and affairs, which examination shall be at the expense of such investment company" and to make an appraisal at the like expense if its properties, including tangible and intangible assets, is utterly unreasonable, and, as applied to the normal business, potentially prohibitive. If we had an act authorizing the executive to examine any business or transaction at the expense of the individual and upon a finding of wrong in the transaction to prohibit it, such an act would be plainly unconstitutional, but it would fall far short of the present prohibition.

This prohibition rests on the dealer offering securities which have not been approved upon the application of the issuing company. It applies to a very large part of the normal business. As applied to any normal investment offering it is plainly prohibitive.

POINT VI.

The Act impairs the freedom of commerce between the States.

1. The unanimity of opinion expressed by the lower courts on this point must be especially persuasive. They have recognized, as this Court has recognized, the fact that an article of purchase and sale between the states is an article of commerce between the states. There would, we presume, be no question on this point but for the forced construction attempted to be placed upon Nathan *v.* Louisiana, 8 How., 73, and Paul *v.* Virginia, 8 Wall., 168. So far as the latter case goes, the distinction is plain between a policy of insurance, which is a contract between the parties having nothing to do with interstate commerce, except that the parties may reside in different states, and the case of stocks and bonds as subjects of interstate sale.

While in Nathan *v.* Louisana, the tax imposed was upon a dealer in bills of exchange, and the dealer in question dealt in foreign bills of exchange, the Court seems to have looked upon the transaction primarily as involving the question of "the right of a state to tax its own citizens for the prosecution of any particular business or profession within the state." The defendant was a citizen of the state, and he would seem to have been unquestionably liable to the tax as a dealer. The tax was not exclusively upon the sale of bills of exchange between the states, nor was the tax upon the bills themselves. It was a tax upon doing the business which was primarily within the state, and was objected to, it would seem, on the ground that some of the business of the dealer was inter-

state. It seems to us that this case is negligible as applied to the present statute.

Dealing with the question as an open question in this Court the interstate sale of securities seems to us to fall clearly within the opinion written by Chief Justice Marshall in Gibbons *v.* Ogden, 9 Wheat., 1, at page 189:

> "Commerce, undoubtedly, is traffic, but it is something more: It is intercourse; it describes the commercial intercourse between nations and parts of nations, in all its branches, and is regulated by prescribing rules for carrying on that intercourse."

In Paul *v.* Virginia, in holding that the issuance of a fire insurance policy in a foreign state was not an interstate commerce transaction, the Court said (p. 183), that insurance contracts

> "are not subjects of trade and barter offered in the market as something having an existence and value independent of the parties to them."

Adding:

> "They are not commodities to be shipped or forwarded from one state to another, and then put up for sale. They are like other personal contracts between parties which are completed by their signature and the transfer of the consideration. Such contracts are not interstate transactions, though the parties may be domiciled in different states. The policies do not take effect—are not executed contracts—until delivered by the agent in Virginia. They are, then, local transactions, and are governed by the local law."

It is evident that the sale of stocks and bonds when issued and offered for sale by a dealer in New York or Chicago to an investor in Michigan,

represents something more than the contract of insurance dealt with in Paul *v.* Virginia. It is a "subject of trade and barter offered in the market as something having existence in value independent of the parties to them," that is, of the parties to the transaction of purchase and sale. "They are not commodities," but it is not necessary that a thing be a "commodity" in order to be a subject of sale or commerce.

The case of International Textbook Co. *v.* Pigg, 217 U. S., 91, is almost, if not quite, on all fours with the present case. The statute in that case was similar, but in some respects not so rigorous as the statute here at issue. The subject of commerce in that case was primarily the intercourse between the parties. The Court, stating that the business of the complainant company was "of a somewhat exceptional character," said (p. 106):

> "It was, in its essential characteristics, commerce among the states within the meaning of the Constitution of the United States. It involved, as already suggested, regular and, practically, continuous intercourse between the Textbook Company, located in Pennsylvania, and its scholars and agents in Kansas and other states. That intercourse was conducted by means of correspondence through the mails with such agents and scholars. * * * More than that; this mode—looking at the contracts between the Textbook Company and its scholars—involved the transportation from the state where the school is located to the state in which the scholar resides, of books, apparatus and papers, useful or necessary in the particular course of study the scholar is pursuing and in respect of which he is entitled, from time to time, by virtue of his contract, to information and direction. Inter-

> course of that kind, between parties in different states—particularly when it is in execution of a valid contract between them—is as much intercourse, in the constitutional sense, as intercourse by means of the telegraph—'a new species of commerce,' to use the words of this court in Pensacola Telegraph Co. *v.* Western Union Telegraph Co., 96 U. S., 1, 9."

There was in this case apparently no purchase or sale of books. There was simply a continuous course of correspondence, and the books were shipped and reshipped as a part of the contract. The "intercourse," not the books, was the primary test of commerce. To have held that the transportation of the books as an incident of the intercourse would make the principle of which it was an incident subject to interstate commerce, would of course, have been unsound. No such view seems to have been entertained by the Court.

2. In the case of Darnell *v.* Indiana, 226 U. S., 390, a tax upon shares of foreign corporations was objected to partly on the ground that it was a tax upon property coming from a foreign State, and therefore was in conflict with the commerce clause, under Darnell *v.* Memphis, 208 U. S., 113. Both counsel seem to have recognized that the stock, when sold, would be an article of commerce between the States. The Court seemed to recognize this contention, but decided the case on the ground that the plaintiffs were not within the constitutional protection sought. In the Memphis case the discrimination had been against the crops and the manufacture of products of other States.

See, also, Champion *v.* Ames, 188 U. S., 321, holding that lottery tickets are articles of commerce.

3. It need, we think, hardly be argued that the prohibition placed both on the business and the transaction of the sale of securities by the present act is, as applied to interstate transactions and to the business of the present appellees, in violation of the commerce clause of the constitution. The burden is direct, and in many cases, prohibitive.

The attempt to rely upon the inspection cases is, we think, hardly serious enough to require an answer. It is one of the fallacies of this legislation that fraud in the issuance and sale of securities can be more readily prevented than can fraud in the sale of tangible property. The contrary we think is the fact. Generally speaking, a defect in personal property may be discovered by inspection. A fraud in the issuance of sale of stocks cannot be so discovered. The inspection of the stock or bond as such means nothing. What is attempted by the statute and what is in principle necessary, is an investigation of all the multitudinous elements entering into the question of the truth or falsity of the representations made in connection with the sale of a stock or the soundness of the enterprise on which it was issued. This inspection may extend to China or Peru, and involve reducing to writing for "inspection" the testimony of many persons. The language of the Court in People *v.* Compagnie Gen. Transatlantique, 107 U. S., 59, at 62, is apt:

> "What is an inspection? Something which can be accomplished by looking at or weighing or measuring the thing to be inspected, or applying to it at once some crucial test. When testimony or evidence is to be taken or ex-

amined, it is not inspection in any sense whatever."

An "inspection" to determine the solvency of a corporation, or the good character of an individual, or the truth of a written statement, as a condition precedent to the right of a corporation to sell its stocks, or the right of the individual to buy or sell stocks, or the right to sell a particular stock, is absurd.

POINT VII.

The Act is unconstitutional and void and the orders below should be affirmed.

This act practically vests, or is intended to vest, in the Security Commission the complete power of government over the issue or sale of all securities except the limited classes exempted under (a)—(g) of Section 3. Should the letter of the act be insufficient in a particular case—in other words, could a finding of fraud not be predicated or even if the Commission could not agree that in its opinion the sale would work a fraud; it can by asserting the power of investigation and the prohibitive expense involved against the applicant, drive him from the State. Such is the substance, purpose and effect of the act. In subjecting the appellees to this autocratic power it destroys their liberty, takes their property, and impairs the freedom of commerce, and at the same time violates the specific prohibitions of the State Constitution.

Respectfully submitted,
GEORGE W. WICKERSHAM,
ROBERT R. REED,
Counsel for named Appellees.

CHARLES K. ALLEN,
Of Counsel.

Appendix.

Bank Supervisor's Proposed Blue Sky Law, with Statement by Committee Appointed by National Association of Supervisors of State Banks. (Italics ours.)

Proposed Blue Sky Act.

Section 1. If any person, including a corporation or association, and the officers or agents thereof, alone or in common with others, having devised or intending to devise any scheme or artifice to defraud by the issuance, sale, promotion, negotiation or distribution of any stocks, bonds, notes or other securities, shall in or for executing such scheme or artifice or in attempting so to do, commit any overt act within the State, such person shall, upon conviction, be punishable by a fine of not more than $5,000 or by imprisonment for not more than *five* years, or by both such punishments, at the discretion of the Court. (Adapted from the Federal Postal Laws, R. S., Section 5480.)

Section 2. Every person, firm, corporation or association, hereinafter called the dealer, who shall, as principal or agent, promote by advertisement, circular, prospectus, or by any other form of public or general offering or through agents, the sale of any securities in this State (except to banks, bankers, trust companies, dealers or brokers in securities), shall, prior to or at the time of making such promotion, notify the (official or Board) of such fact, describing such securities, and file from time to time any and all prospectuses and circulars, if any, used or to be used in such promotion, and such (official or Board) may

make such investigation thereof and require such information or proof with respect thereto as (he) may deem necessary to determine the character of such securities and of such promotion. If any such dealer shall mail, postpaid and properly addressed to the (official or Board), a prospectus or circular containing the offiering of any such securities, with the name and address of such dealer, the same shall be deemed a notification under this section of the promotion thereof as aforesaid.

Section 3. The provisions of Section 2 shall not apply to the offering or sale of any securities on any recognized exchange in this State, nor to the advertisement or sale thereof at public auction or pursuant to the order of any Court, nor to the advertisement of any securities in any magazine or newspaper published outside of the State, unless the dealer shall cause the same to be distributed in the State.

Section 4. Such (official or Board) may also make such special investigation as may be deemed necessary, in connection with the promotion of any securities under this act, to determine whether the same constitutes a violation of this act by any individual corporation or association, and such (official or Board) shall have the power to issue subpœnas and process compelling the attendance of any person and the production of any papers and books for the purposes of such investigation and examination, and shall have power to administer an oath to any person whose testimony may be required on such examination or investigation.

Section 5. If such (official or Board) shall determine that any such promotion constitutes a violation of this act, (he) shall immediately take such steps as may be necessary to cause the arrest and prosecution of all persons deemed guilty thereof. It shall be the duty of any District Attorney to prosecute any violation of this act in his county and upon request of the (official or Board) the Attorney-General shall direct and control such prosecution.

Section 6. Any person who shall knowingly make or file or cause to be made or filed any statement, information or proof required hereunder by such (official or Board), which is materially false, or who shall promote or cause to be promoted by advestisement, circular, prospectus or by any other form of public or general offering or through agents, the sale of any securities, without complying with Section 2, except as therein excepted, or without furnishing to the (official or Board) any information or proof in the possession of or reasonably obtainable by such person, if and after the same are required by the (official or Board) under such section, shall upon conviction, be punished by a fine of not more than $1,000, or by imprisonment for not more than one year or by both such punishments, at the discretion of the Court.

Section 7. Every dealer in securities, including every person, firm, corporation or association engaged in the business of selling stocks, bonds, notes or other securities, having a place of business in this State, shall annually on the first day of , file with the (official or Board) a statement showing the name and busi-

ness address in the State of such dealer and if the principal office of such dealer is out of the State, the address of such principal office, and if such dealer is a corporation or association organized under the laws of another State the address of the principal office of such corporation in such State. Such statement shall be accompained by a filing fee of twenty-five dollars . Every agent of any such dealer not having an office in this State or not having filed such statement as aforesaid, who shall in this State offer or sell any such securities, shall, annually on the first day of or thereafter, and before he shall in this State offer or sell any such securities, file a statment with the (official or Board) showing the name of such agent and his address if any in this State and the name and principal office of any such dealer, and if such dealer is a corporation or association organized under the laws of another State, the address and principal office of such corporation in such State. Such statements shall be accompained by a filing fee of three dollars. A violation of this section shall be punished by a fine not exceeding $500.

STATEMENT OF COMMITTEE.

To the National Association of Supervisors of State Banks.

A resolution was adopted at the last annual Convention of the National Association of Supervisors of State Banks, reciting "that inasmuch as the operation of the Blue Sky Law in different States has met with uncertain results, therefore be it resolved that this Association offers to co-operate with the so-called investment bankers to secure uniform laws which will be practical in effect."

The undersigned Committee was appointed pursuant to this resolution. It presents herewith a proposed law which embodies what seem to it to be the fundamentals, so to speak, of an effective and constitutional blue sky law. These features are:

1. A fraud provision adapted from the existing Federal law. Such a provision should in our opinion be the basis of any legislation on this subject. *Without it, a blue sky law may serve to ward off obvious frauds: it cannot be a deterrent and is in fact an aid to more skilful frauds which are not detected in the first instance.*

2. A provision requiring that a State official be notified of all offerings of securities made within the State. This publicity feature has, we believe, been the cause of the great success of the Kansas type of law, and for it credit is due to the originators of that law. It compels every promoter to make his presence and purpose known. This requirement standing alone is practically prohibitive of two-thirds of the frauds.

3. Provision giving general power of investigation to the State official to uncover fraud in any promotion *This provision has been devised by the Committee to meet all kinds of instances.* The Committee does not believe it advisable for the statute to attempt to specify either the procedure or proof necessary to uncover fraud. There can be no rule applicable to all cases, and the requirement of some matters suggests the exclusion of others. There could not be uniformity in practice, and it is not wise to attempt it in a statute covering so large a field.

We believe this proposed law is capable of enforcement, and incapable of evasion. It does not purport to give the sanction of the State to any

offering. *It does not make the offering subject to State approval, but it puts the State in a position where if the offering is fraudulent, it can be stopped in the most effective way, i. e., by prosecution.*

We do not believe ingenious stock frauds can be prevented by requiring them to obtain a State license; there being no penalty attached to the making of the application, and the license if granted being in fact a material aid to the fraud

We do believe that all fraud can be prevented by making it unprofitable, that is, by imposing heavy penalties upon it and providing adequate machinery for its detection and punishment.

The proposed law, however, speaks for itself. It is plain reading, based on a general principle, and puts the whole matter with plenary power in the hands of the State, the prosecutor, the Court and the jury.

Dated, New York, January 27th, 1915.

EUGENE LAMB RICHARDS,
Chairman.

WM. H. SMITH,
GEO. M. LA MONTE,
Committee on Blue Sky Legislation
of National Association
of Supervisors of State Banks.

OCT 1 1916
JAMES D. MAHER
CLERK

IN THE SUPREME COURT OF THE UNITED STATES

October Term, 1916

No. 413

FRANK W. MERRICK, JOHN W. HAARER AND GRANT FELLOWS,

Appellants,

vs.

N. W. HALSEY & COMPANY, ET AL, AND WEIS FIBRE CONTAINER CORPORATION,

Appellees.

BRIEF FOR APPELLEES.

WEIS FIBRE CONTAINER CORPORATION, WM. P. BONBRIGHT & COMPANY, WILSEY, FIERLIEN COMPANY, OTIS & COMPANY, BOLGER MOSSER AND WILLIMAN

HAL H. SMITH,
Attorney for the Above Named Appellees.

DETROIT:
CONWAY BRIEF CO., 142-150 LAFAYETTE BOULEVARD
1916

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INTRODUCTION.

The statement of the appellants as to the parties to this litigation and as to the pleadings is correct. It should, however, be pointed out that the bills of complaint assert-

ed that an irreparable injury would result to the plaintiffs by reason of the enforcement of the act and that the affidavit filed with the bill (see Rec. p. 88) and the intervening petitions likewise showed that irreparable injury would result if the act were enforced against the plaintiffs and the interveners. It was on the motion for the preliminary injunction that Judges Dennison, Sessions and Tuttle held the act to be invalid and unconstitutional and it was from the order directing that such preliminary injunction issue that the appeal is taken (Rec. p. 108). The assignment of errors (Rec. pp. 109-111) include assignments directed to the question of the jurisdiction of the court, and as to the showing of the plaintiffs of irreparable injury. Assignment No. 8 alleged that "the Court erred in holding and adjudging that said proceedings are not suits against the State of Michigan." The Appellants now make no question as to the jurisdiction of the Court, nor as to the showing of irreparable injury, nor do they insist that the suit is one against the State of Michigan. The questions raised upon this appeal are, therefore, directed solely to the invalidity of the statute as to whether or not it violates constitutional rights.

In the brief of Appellants at page 73, it is asserted that there is no allegation in the bill of complaint that the plaintiffs do not maintain offices in the State of Michigan and that no claim is made that the securities handled by the plaintiffs are brought into the state and sold in "original packages." The bill of complaint of the dealers N. W. Halsey & Company et al did assert (Paragraph 6, Rec. p. 3) that these plaintiffs send their agents into the State of Michigan and that these agents there solicit orders which they transmit to the offices of the plaintiffs outside the State of Michigan and that the securities so ordered and purchased were forwarded direct to the purchaser in Mich-

igan from the offices of the plaintiffs without the State of Michigan. The bill of complaint of the Weis Fibre Container Corporation (Rec. p. 35) does not include this allegation. This plaintiff is a manufacturing corporation and it has complied with the statutes of Michigan permitting it to do business therein. The petition of Otis & Company for intervention, which is typical of the other petitions, asserts (Rec. p. 92, paragraph 4) that this company sends its agents into Michigan to solicit the sale of securities and that these agents transmit orders they receive to the office of the petitioner in Cleveland, Ohio, and that "thereafter a delivery of such securities is made by such petitioner in interstate commerce," to the purchaser thereof in the State of Michigan.

It is our position that it was not necessary to formally deny that any of the plaintiffs and interveners had an office within the State of Michigan or to specifically assert that when the securities, for which their agents had transmitted orders to the office outside the State, were delivered in the State of Michigan they were so delivered in "original packages," within the meaning of the original package liquor cases.

Synopsis of Argument.

We shall not attempt in this brief to answer categorically the argument of the Attorney General, but shall content ourself with analysing the act in question and the objections against it as we see them. We shall emphasize the fundamental objections to the law. We do not mean that the act should not be destroyed if it offends in any way against the Constitution. The rights of the plaintiffs demand that result. But we do desire that the basic theory upon which the law stands be emphatically condemned. The argument, therefore, falls under the following heads:

1.

The act, the Blue Sky Law of Michigan, is not a valid exercise of the police power. It is a clear and unmistakable infringement on constitutional rights.

II.

The State, in the exercise of its police power, has no right to prohibit interstate trade in legitimate articles of commerce. Stocks, bonds, and securities, as defined by this law, are legitimate articles of commerce. The traffic in these articles between several states is interstate commerce. This law prohibits, burdens and regulates this traffic, and is therefore in conflict with the Federal Constitution.

III.

The Statute vests an arbitrary power in the Commission. The rule by which the Commission is to approve or disapprove securities presented to it is the opinion of the Commission that the sale of such securities will work a fraud. To confer upon the Commission the power to regulate the sale of the securities described in the act according to its arbitrary opinion subjects those securities to the practically uncontrolled discretion of the Commission, and the act for this reason is invalid.

IV.

The title to the act covers more than one object and does not express the objects set forth in the Statute. It, therefore, offends against Section 21, Article 5 of the Constitution of the State of Michigan.

V.

The Statute is class legislation, and is, therefore, void. It discriminates as between securities of the same character and the same class.

VI.

The Act delegates to the Michigan Securities Commission legislative authority and it is void for that reason.

VII.

The act confers upon the Securities Commission judicial power. It is, therefore, in violation of the Constitution of the State of Michigan.

VIII.

The law cannot accomplish its purpose. The commercial situation as described by the appellants offers no justification for a law of this character, nor for this particular statute. A multiplicity of ill-considered statutes of the same general character as this law furnishes no argument sustaining the Michigan Blue Sky Statute.

An Analysis of the Blue Sky Law.

The counsel for the appellants has included in his brief the entire of the Act in question here, but a brief analysis of its provisions will not, we think, be out of place.

Act 45 of the Public Acts of Michigan of 1915, the so-called "Blue Sky Law" purports to regulate so-called "investment companies," their securities and persons dealing therein. "Investment companies," as defined by the Act, includes "every person, corporation, co-partnership, company or association" which shall either himself, themselves or itself, or by or through others, sell or negotiate for the sale of any stocks, bonds or other securities issued by him, them or it, within the State of Michigan.

The securities of this or any other State, or of municipal corporations, state and national banks, trust companies, "public or quasi-public corporations," corporations not for pecuniary gain, are exempted from the Act. So also are mortgages on real or personal property situated within the state where the entire mortgage is sold in one sale.

An "increase of stock sold and issued to stockholders" and stock dividends are exempted, as are "securities listed in any standard manual of information approved by the Commission. Unsecured commercial paper is likewise exempted.

The term "investment companies" includes all persons and corporations which issue stocks and bonds, and therefore includes all manner of business enterprises, manufacturing, mining, land-owning, mercantile and farming, should any such enterprise issue securities and sell them in Michigan.

The Act creates the Michigan Securities Commission to consist of the State Treasurer, the Commissioner of the Banking Department and the Attorney-General of the State.

The "investment company," before selling, offering for sale, taking subscriptions for or negotiating for the sale in any manner of the securities of its own issue not exempt under the Act, must

(a) File with the Securities Commission

1. "A statement showing in full detail the plan upon which it proposes to transact business."

2. "A copy of all contracts, stocks, bonds, or other instruments which it proposes to make with or sell to, its contributors or customers."

3. A copy of its prospectus and of the proposed advertisements of its sale of stocks, bonds and other securities.

4. A statement which shall show the name and location and head office of the "investment company" and the names and addresses of its officers.

5. An itemized account of its financial condition and the amount of its assets and liabilities?

6. Such other information touching its condition and affairs as the Commission may require.

7. If it be a co-partnership it shall file a copy of its articles.

8. It it be a corporation, a copy of its articles, constitution and by-laws.

9. If it be organized under the laws of another state, it must file, in addition, a certificate that it is entitled to transact business in Michigan.

(b) Pay a filing fee of one tenth of one per cent on the face value of the securities, such fee to be not less than Ten Dollars, nor more than One Hundred Dollars. (Sec. 4.)

(c) File its consent, if it be a foreign "investment company" that actions may be begun against it by service of process on the Commissioner of Banking. (Sec. 6.)

(d) Submit, at the option of the Securities Commission, to an examination of all its business and affairs at its own expense. (Secs. 8 and 13.)

(e) Register all its authorized agents with the Securities Commission (Sec. 12) and pay fees therefor.

After conforming to the Act and the requirements of the Commission, the "investment company" must further:

(a) File each January a detailed report of its condition and such other information as may be required by the Commission (Sec. 21).

(b) Keep its accounts in a certain prescribed manner (Sec. 13).

(c) Keep its books of account open to the Commission.

(d) Permit any information in regard to its business to be furnished to the public by the Commission (Sec. 16).

(e) Permit a further examination, at the will of the Commission, and pay the fee therefor, whenever the Commission deem it advisable.

After the filing of the application and compliance with the terms of the Act, it is still unlawful for the "investment company" to sell or offer for sale its securities until permission is given by the Commission, and this permission or approval is only to be obtained after a hearing. If the application is filed more than twenty-four hours before the monthly meeting of the Commission, it is heard at the next regular monthly meeting. It may be heard at a special meeting on two days' notice to the applicant (Sec. 7).

The Commission *may adjourn these hearings at its will,* may ask for further information and may make a detailed examination of the Company's affairs and an appraisal of its property (Sec. 8).

There can be no dealing in the securities on which the application is filed until they have been approved by the Commission, and no time is fixed in which that approval must be given. There is, therefore, a period of suspense during which sales of securities otherwise lawful are prohibited, and the length of this period rests solely in the convenience or whim of the Commission.

As already noted, the Commission may, before approving the securities of any applicant, not only examine its affairs and summon its officers to testify under oath. It may also *appraise* the applicant's property (if it be a corporation). (Sec. 8) and fix the amount of securities which the company may issue in payment for the transfer of "property, patents, good-will, promotion and intangible assets." The appraisal shall be at the expense of the Company (Sec. 8). How it would be accomplished if the Company were a non-resident of Michigan is not set forth in the statute. The Commission may withhold the permission to sell until any excess of securities over its valuation of the property transferred for same has been either delivered and canceled or placed in escrow (Sec. 8).

The Commission, upon the hearing and examination of the applicant, must disapprove the securities if it finds that the proposed plan of business of said investment company, or its proposed contracts, stocks, bonds, or other securities, *are fraudulent or are of such a nature that the sale of such contracts, stocks, bonds or other securities would, in the opinion of the Commission, work a fraud upon the purchaser.*

If the Commission does not so find, it issues its certificate in the form set out in the statute (Sec. 9), as follows:

> "This is to certify that the.....has this date been given permission to sell $.....
> of its.....within the State of Michigan.
> stocks, bonds or securities
> The Commission does not recommend the purchase of this security."

A violation of the Act by the "investment company" or any other person is made a misdemeanor and is punished by a fine of not more than One Thousand Dollars or imprisonment in the county jail for not more than one year, or both such fine and imprisonment (Sec. 23).

The Act also defines "dealers in such securities" and prohibits any such dealer selling or offering for sale any securities covered by the Act (Sec. 10), unless and until he shall:

(a) File a list of such securities with the Commission (Sec. 10).

(b) Register with the Commission (Sec. 11), and furnish it with certain information.

(c) Pay a registration fee.

(d) File, if a non-resident, an appointment of the Banking Commissioner as his agent to receive service of process.

(e) Pay a fee for each agent.

When a dealer has so complied with the Act, he will receive a license from the Commission (Sec. 11), but he can-

not sell the securities of any investment company unless such company and such securities shall have complied with the Act and been approved by the Commission (Secs. 14 and 15). The dealer himself, however, if the investment company has not complied with the Act, may make application for the approval of the securities (Sec. 15).

The dealer, therefore, is prevented from selling the securities defined by the Act except under extraordinary restrictions and regulations and a sale by a dealer, in violation of the Act, of any securities covered by the Act is made a felony (Sec. 23).

ARGUMENT.

The Police Power and this Act.

THIS ACT, THE BLUE SKY LAW OF MICHIGAN, IS NOT A VALID EXERCISE OF THE POLICE POWER. IT IS A CLEAR AND UNMISTAKABLE INFRINGEMENT ON CONSTITUTIONAL RIGHTS.

We desire here, before we discuss the objections against the Act so far as the police power is concerned, to emphasize that the law is not directed at any single occupation or business. It attempts to regulate the issue of securities by any individual person, partnership or corporation in any and all business enterprises.

Dealers in securities are regulated it is true and to that extent the business of dealing in investment securities is regulated. But the regulation of the dealer and his

calling is incidental to the main purpose of the Act which is the regulation and prohibition, unless in compliance with the Act, of the issue of stock and bonds by corporations and the making of loans in certain forms by individuals, co-partnerships and associations. The burden of the law falls somewhat upon the dealer but its heaviest load rests upon the issuer of the stocks, bonds or securities and the issuer may be any person, corporate or otherwise, engaged in any business whatever, except only the exempted classes.

Clearly there is no such thing as the business of making loans, the business of issuing bonds, the business of issuing stock as applied to the entire business world. These acts are the incidents of any occupation and any business.

At the outset we must therefore differentiate this law from those regulating corporate organizations and fixing the terms upon which a corporation may do business, since this law applies to individuals and co-partnerships as well as to corporations.

We must separate it also from laws regulating those engaged in certain callings which have always been more or less within reach of the police power, such as employment agents and brokers. We must differentiate it also from laws regulating certain business affected with the public interest such as the banking or insurance business, since this law does not segregate any certain business but rather attempts to reach all businesses. And it can hardly yet be said that any business which issues stock or makes loans in the form described by the Statute is affected by the public interest.

Here, however, we touch upon the gist of the appellant's argument. We understand that their position must be, in the last analysis, that any business becomes affected by the public interest so that the police power may prohibit or regulate it, when it offers to any part of the public any stocks, bonds or other securities for sale "in the course of continued and successive transactions of a similar nature."

If this be so all business enterprises must be said to be, at one time or the other, "affected by the public interest." Certainly all large business enterprises would be so affected and that without any wish of their own since the public eagerly deals in their securities, whether they offer them for sale or not.

But this application cannot be made of the phrase "affected by the public interest." That phrase and the consequent exercise of the police power must be limited to occupations, callings, businesses which, by their individual inherent nature are more closely related to the public welfare than are others. And it cannot be applied to an incident of all business and one which may arise at any time in the farming business, the manufacturing business or the investment business.

If this distinction is sound, and we believe it is, it relieves us of the necessity of reviewing the arguments of the appellants which are based on cases referring to specific callings and occupations.

Some better and broader reason must be found for sustaining the law.

We call attention to these matters at the outset because if we were to criticize in any way the excellent brief of

the appellants, we thing we would suggest that it always keeps it clear that the law applies to individuals as well as to corporations and to all manner of business as well as that of the dealer in corporate securities.

The issue and sale of securities is a part of the freedom guaranteed by the 14th amendment to the Federal Constitution and by the Constitution of Michigan.

The State does not contend that the right to issue and sell stocks, bonds and other securities is not a part of the liberty guaranteed by the Constitution. The issue and sale of these securities is in effect the making of contracts "proper, necessary and essential" to the pursuit of lawful livelihoods or avocations.

Allgeyer vs. Louisiana, 165 U. S. 578;
Kuhn vs. Detroit, 70 Mich. 537;
People ex rel Valentine vs. Circuit Judge, 124 Mich. 164.

This Act, by its prohibition of the sale of securities until the permission of the Commission and by its extraordinary restrictions upon the right to issue and sell such securities impairs the freedom guaranteed by the Constitution.

There is no question but that the Act does interfere with the right to issue and sell securities.

The Act absolutely prevents the sale of securities by the issuer thereof or by a dealer therein except upon the permission of the Commission.

The right to issue stock, to execute bonds and to secure their payment by the pledge of property is of no value unless the stock and bonds can thereafter be negotiated. This the law prevents except under heavy restrictions.

The law lays its burden not only upon the specific transaction and the particular investment company. By its sweeping definition of investment companies, it regulates all manner of business enterprises and all kinds of manufacturing and mercantile pursuits.

The burdens of the law are fourfold: the requirement as to the application; the payment of fees; the privilege of inspection, examination and appraisal; and the suspension of the right to sell or dispose of the securities, even though lawful, until the permission of the Commission is forthcoming.

The requirement as to the application is in itself burdensome. It includes not only a complete statement of the applicant's financial condition and copies of its articles, but also a consent that it may be sued in Michigan by service on the Commissioner of Banking. If the applicant is an individual or a co-partnership, a substantial right has been taken away.

Moredock vs. Kirby, 118 Fed. 180.

The fees prescribed by the Act may or may not be onerous according to the financial status of the applicant, but they are fees "for the right to carry on business" and if the business be legitimate, are not within the right of the Legislature to impose.

People ex rel Valentine vs. Circuit Judge, 124 Mich., 664.

The right of the Commission to examine, inspect and appraise is extraordinary. The cost of such examination and appraisal is to be paid by the Company and no limit is set upon it. As the lower court said (Rec. p. 102):

> "There is no limit to either the time which may be consumed or the amount of expense which may be imposed."

The suspension of the right to dispose even of a perfectly lawful and valid security until the Commission's finding is made is the most burdensome of the extraordinary restrictions of the statute.

In the 1913 Michigan Statute, it was provided that a period of thirty days must elapse from the date of the application during which all dealing was suspended. At the expiration of that period, if the Commission had not denied permission, the sales could begin. This definite suspension was condemned by the Court.

Alabama, etc. Co. vs. Doyle, 210 Fed. 173

The new statute substituted a provision forbidding any transactions until the affirmative finding and consent of the Commission, but fixed no limit to the time during which the finding can be delayed. As the lower court observed:

> "This change in the law has not diminished this burden in directness or in weight."

Are these burdens and restrictions within the police power?

These extraordinary burdens and restrictions upon business transactions otherwise lawful are justified by the state as a proper exercise of the police power. It is argued that the purpose of the statute is to prevent fraud, that that purpose is lawful and that the restrictions in the statute contained are proper to accomplish this end.

The purpose of the statute, however, is not to regulate fraud, but rather to prevent financial loss.

The history of the statute is here instructive and conclusive. The statute is a substitute for the Act of 1913, which was declared invalid in *Alabama, etc. Co. vs. Doyle*, 210 Fed., 173. In that statute the final test to be applied to the security was whether or not it would "in all probability result in a loss to the purchaser." The Court condemned this statute and particularly this provision, saying:

> "The element of fraud is wholly eliminated from this part of the statute and all the dependent police power to protect the citizen against fraud must concurrently disappear. No definition of the police power which we have seen or which the industry of counsel has found is broad enough to cover such prohibition and we are aware of no consideration which even plausibly supports its validity."

It was to meet this objection that the 1915 law attempted to modify the tests to be applied by the Commission and the new statute is therefore quite frankly a recognition by the Michigan Legislature that it has no right to regulate financial loss.

The test of the approval of the Commission is now not "the probability of loss," at least so states the statute, but the "probability of fraud." The words "to prevent fraud in the sale thereof" in the title to the former Act now appear at the beginning of the new title "An Act to prevent fraud in the sale," etc. But has the real standard of the Commission's action been changed? So long as the ostensible test is *probability* can it be in reality anything but *probability of loss?* How can the Commission determine any other probability? Loss may be the inevitable result of the nature of the security. But there can be no fraud without deception. How can the Commission pass on the future intention of the seller and the future knowledge of the buyer?

There is, however, one new section in the law which deals exclusively with the probability of loss and as the lower court pointed out makes clear the meaning of the phrase in the "opinion of the Commission work a fraud on the purchaser." Section 8 provides for the appraisal of property turned over to a corporation to pay for its stock. "It may fix the amount of stocks, bonds and securities that shall be issued by any corporation, foreign or domestic, in payment for property, etc." * * * And said Commission may withhold its license to sell such stocks and bonds and securities if such corporation has issued stocks, bonds and securities in payment for property, etc., *in excess of their value.*

This surely has no relation to the probability of fraud and it is the key to the whole statute. The Act is still directed to financial loss and the probability of loss still remains the test of the Commission's action. The Commission is in effect to fix the price at which securities are to be sold so that not only fraud but *loss* may be prevented.

But let us assume for the sake of argument that the real purpose of the law is the protection of the public against fraud and not against loss. Before we can even then sustain the act, we must still inquire whether or not the fraud there referred to is proper object for the police power. Can the occasional fraud, that fraud which arises in the individual transaction justify a law regulating the business of which the single transaction is a part? Or must it be fraud which is incidental to the business, a fraud which the business itself, from its character and the manner in which it is generally conducted invites and encourages.

It should be remembered that the proposal is not to regulate certain kinds of business but all business when it

issues and sells securities not in the exempted classes. It is not to regulate certain persons doing certain business, but all persons doing the acts described.

Regulation of all business for the purpose of reaching the occasional fraud is clearly not justified. The fraud must be necessary incident to the particular business, or the business must lend itself particularly easily to deception, else the business cannot be regulated—only the fraud therein.

> "It is a novel legislation," said Justice Parker in *People ex rel. Tyroler vs. Warden*, 157 N. Y. 116, "indeed, that attempts to take away from all the people the right to conduct a given business because there are wrongdoers in it."

To say that there is a necessity for such a law affecting substantially every issue and negotiation of corporate stocks or evidences of debt is to indict all business and all business men as fraudulent.

This law subjects to the Commission's authority all secured commercial paper. Will the Court, bearing in mind the tremendous volume of this form of security and the great part it plays in all commerce, say that it is so commonly fraudulent as to require this regulation? The mere statement of such a possibility is absurd.

The law regulates the issue and sale of corporate securities. The corporation is today the prevailing form of business organization. Corporate capital stock is the universal and convenient method by which a great per cent of our business property is generally represented and bought and sold. The corporate bond and mortgage is the familiar and general way of securing the long time loan. Both the stock certificate and the bond pass freely as negotiable, or quasi-

negotiable instruments. The statutes authorize investments in them by trustees and savings banks. To now say that all corporate business and these securities are so frequently the vehicles of fraud and lend themselves so easily to deception that their entire issue and all their sale must be regulated as this law regulates them, is to declare the very basis of modern business to be fradulent.

To paraphrase the language of this Court in *Tanner vs. Little*, 240 U. S. 369, we may assume that this statute was "enacted upon a belief of evils." But surely that belief is "arbitrary" if it imputes the widespread fraud which must be assumed to justify such a wholesale regulation of modern business.

The language of the lower court in the case on the 1913 law cited supra, is extremely pertinent.

> "When we thus recall that the prohibition applies to a private business, the question at once presents itself whether frauds and opportunities for fraud sufficiently characterize the business to justify its entire prohibition save under drastic restrictions. We cannot shut our eyes to the fact which all men know that, as compared with the total dealings in securities covered and contingently prohibited by this act, those which may fairly be suspected to be of a fradulent character are a very trifling proportion; and there is no reason to suppose that the percentage of fraud is any greater than in each of the ordinary business and professional occupations."

The words of the Michigan Supreme Court in *People ex rel. Valentine vs. Circuit Judge*, 124 Mich. 664, cited by the lower court are no less in point.

> "The business of buying and selling on commission has existed ever since commerce began. There

are and always have been dishonest men engaged in it, as there are and always have been in every other branch of business. There are and always have been dishonest sellers, who will pack their produce in such a manner as to deceive. It would be as reasonable to require the latter to give bond to properly pack their produce. In every such case the common law provides an ample remedy for redress to the injured party for breach of contract. There is no more reason why a commission merchant should pay a license fee, and execute a bond to pay his debts and to do his business honestly, than there is that any other merchant should pay a like fee, and file a like bond to properly do his business and pay his debts. The business requires no regulation, any more than any other mercantile pursuit. There is nothing in it hostile to the comfort, health, morals, or even convenience, of a community. It is carried on by private persons in private buildings, and in a manner no different from that in which the merchant selling hardware or groceries or dry-goods carries on his business. The law can find no support in the police power inherent in the State."

But it is urged that in view of the action of the Legislature, the Court has no power to determine for itself that no necessity exists for this statute. This we do not admit.

We shall not discuss at length the power of the Legislature to bind the Court in this respect. There is of course a line beyond which the lawmaking power cannot go—and within which the judicial power is supreme.

In *People vs. Smith*, 108 Mich. 527, the Michigan Court asserted its right to review, under certain conditions, the determination of the Legislature as to the necessity of police power legislation.

In discussing the validity of a law regulating the use of emery wheels, it said:

> "Each law of the kind involves the questions: (1) Is there a threatened danger? (2) Does the regulation invade a constitutional right? (3) Is the regulation reasonable? * * * All, then, seems to be embraced in the question of necessity. * * * If the Courts find the plain provisions of the Constitution violated, or if it can be said that the act is not within the rule of necessity in view of facts *of which judicial notice* may be taken, then the act must fall."

We are content to accept to the fullest extent the holding of this Court in *Rast vs. Van Deman & Lewis Company*, 240 U. S. 342, and to admit that there does exist in the Legislature the power "to regulate conduct and contracts and in the exercise of the power to classify objects, upon its conception of the public welfare, the right of review to be exerted by the Courts only when the legislation is unreasonable or purely arbitrary."

We insist that this law should be condemned by the Courts under the application of this rule. We submit that the Court must say that the Legislature has here overstepped the bounds of its power. The Court acting on its own knowledge cannot assert that modern business is so generally fraudulent that this regulation is necessary for the public good, and it should say that the legislation is both "unreasonable and purely arbitrary."

But even if the Court should yield to the Legislature the right to so indict the business world as fraudulent and should consent that the Legislature's decision as to the necessity for the law was final, there still remains the question as to whether the restrictions in the statute are not arbitrary and unreasonable.

Such a statute to be valid must not only have a relation to the public welfare but it must not be unreasonable. There might in other words be an evil which needed correction but the effort to correct it might unreasonably destroy rights; it might be an "arbitrary and oppressive interference with the right of contract."

We submit that the restrictions and burdens of this statute do so arbitrarily and unnecessarily interfere with constitutional rights.

The statute absolutely suspends the issue, negotiation and sale of the securities for a period limited only by the whim of the Commission. The complete honesty in the transaction, the highest value in the security, cannot obviate the operation of the statute to prevent the issue or sale thereof.

Must all honest business where loans are negotiated and corporate securities sold be suspended for even one day to permit the Commission to investigate the probability of fraud? And how can any time limit be set upon the right to honestly buy and sell? We insist that any such limitation is vicious and beyond any theory of the police power. The ordinary course of such business does not yet carry any such badge of fraud so that this restriction is required.

The provision of Section 8 for an appraisal is another requirement so unreasonable and drastic as to be beyond the power of the State. As to corporations organized within Michigan the State has already set its seal of approval on the payment of property for stock. The oath of the incorporators is required as to values and the property must be of a certain kind and be itemized in the articles. Now comes the Securities Commission to appraise the property, take the stock into escrow, or demand its cancellation or deposit before it can be sold. A single stockholder attempt-

ing to sell his stock through a broker or dealer could involve all the others in litigation and loss. The approval of the State on the company's charter would be set aside and good faith purchasers of the securities caused both loss and embarrassment.

The requirement that all foreign investment companies must consent to the jurisdiction of all the courts of the state is another unreasonable restriction. It is settled that a corporation cannot be required to so submit itself.

Sioux Remedy Co. vs. Cope, 235 U. S. 197.
Buck Stove Co. vs. Vickers, 226 U. S. 205.

As to non-resident individuals the law is equally clear. It violates the constitutional right of such non-residents by depriving them of the immunity or exemption allowed to citizens of this State, since citizens of Michigan must be sued by personal service.

Moredock vs. Kirby, 118 Fed. 180;
Caldwell vs. Armour, 1 Penn. (Del.) 545;
See 9 Fed. Statutes, Ann. p. 176.

The law cannot be defended as a licensing law or an inspection statute.

We now turn to the theories of the defense of the law. It is asserted that it is a licensing law. It provides for a dealer's license and there is an effort to use in its language the "nomenclature of a license law." But there is no similitude in its essentials to a license act. It deals with individual transactions. While the investment company receives a certificate of approval on each issue of securities there is no license to permit it to issue other securities. There is only the single approval. A new application must be made on each new security. The test of the permission is not the character of the dealer or his solvency.

It is the character of the security. The dealer is not licensed. The dealer who is licensed can sell only approved securities.

Nor is this Act an inspection statute though there has been an insistent effort to bring it within that definition.

The Supreme Court of the United States in *People vs. Compagnie Gen. Transatlantique,* 107 U. S. 59, defined inspection and denied the constitutionality of a New York Statute for the "inspection" of immigrants.

Justice Miller said:

> "What is an inspection? Something which can be accomplished by looking at or weighing or measuring the thing to be inspected, or applying to it at once some crucial test. When testimony or evidence is to be taken or examined, it is not inspection in any sense whatever."

In *Gibbons vs. Ogden,* 9 Wheat 1, 203, the Court limited inspection laws to articles of food, agriculture and manufacture. They have never been extended beyond the inspection of tobacco, *Turner vs. Maryland,* 107 U. S. 38; of butter, *Plumley vs. Mass.*, 155 U. S. 461; flour, *Voight vs. Wright*, 141 U. S. 62; hides, *Neilson vs. Garza,* 2 Woods 287; fertilizer, *Pataspsco Guano Co. vs. North Carolina*, 171 U. S. 345; cattle, *Minnesota vs. Barber,* 136 U. S. 313.

In the recent case of *Sligh vs. Kirkwood*, 237 U. S. 52, 59, the same definition is clearly indicated:

> "The power of the State to prescribe regulations which shall prevent the production within its borders of impure foods, unfit for use, and such articles as would spread disease and pestilence, is well established. Such articles, it has been declared

> by this court, are not the legitimate subject of trade or commerce, nor within the protection of the commerce clause of the Constitution. 'Such articles are not merchantable; they are not legitimate subjects of trade and commerce. They may be rightly outlawed as intrinsically and directly the immediate sources and causes of destruction to human health and life. The self-protecting power of each State, therefore, may be rightfully exerted against their introduction, and such exercises of power cannot be considered regulations of commerce prohibited by the Constitution.' *Bowman vs. Railway Co.*, 125 U. S. 465, 489."

We conclude our inquiry into the relation of this law to the police power by inviting the Court to read the words of the Supreme Court of Michigan in *People ex rel. Valentine vs. Berrien Circuit Judge*, 124 Mich. 664.

In this case the Court considered a law requiring "persons, firms and corporations who hold themselves out as commission men, brokers, agents, or merchants and their agents, to give bonds to pay their debts." The opinion is brief and we quote it in toto:

> "Grant, J. (*after stating the facts*). Acts of this character, when valid, must find a reason for their existence in the police power of the State. The act is not aimed at brokers, in the ordinary meaning of that word. It is not aimed at commission merchants generally. It is aimed solely at commission merchants who engage in the business of selling farm produce for producers upon commission. It provides that such a merchant shall pay a fee and execute a bond, as conditions precedent to doing business. The condition of the bond is the honest and faithful performance of his contracts. The

business of buying and selling on commission has existed ever since commerce began. There are and always have been dishonest men engaged in it, as there are and always have been in every other branch of business. There are and always have been dishonest sellers, who will pack their produce in such a manner as to deceive. It would be as reasonable to require the latter to give bond to properly pack their produce. In every such case the common law provides an ample remedy for redress to the injured party for breach of contract. There is no more reason why a commission merchant should pay a license fee, and execute a bond to pay his debts and to do his business honestly, than there is that any other merchant should pay a like fee, and file a like bond to properly do his business and pay his debts. The business requires no regulation, any more than any other mercantile pursuit. There is nothing in it hostile to the comfort, health, morals, or even convenience, of a community. It is carried on by private persons in private buildings, and in a manner no different from that in which the merchant selling hardware or groceries or dry-goods carries on his business. The law can find no support in the police power inherent in the State. It is not like the liquor traffic, which, under the decisions of every court, is subject to the police power, because of the injury it does to the health, morals, and peace of the community, and may be prohibited altogether. Neither is there anything in it requiring regulation, as do hack-drivers, peddlers, keepers of pawnshops, and the like. The legislature of this State is not empowered by the Constitution to regulate contracts between its citizens who are engaged

in legitimate commercial business, or to require any class of persons to pay a fee for the right to carry on business, or to give a bond to perform their contracts which other parties may choose to make with them. The Constitution guarantees to citizens the right to engage in lawful business, unhampered by legislative restrictions, where no restrictions are required for the protection of the public. We are compelled to hold this law void, because (1) it is class legislation, and (2) it is an unjustifiable interference with the rights of citizens to carry on legitimate business.

"It is unnecessary to discuss the other questions raised. The writ is denied.

"The other Justices concurred."

It may, perhaps, be of some service if we should classify the cases which are cited by the appellants as sustaining its theory that this law is within the limits of the police power. The appellants rightly concede that no law of this precise character is yet upon the statute books and insist very properly that the limits of the police power cannot be accurately defined but must be, to quote the words of Justice Holmes in *Noble State Bank vs. Haskell*, 219 U. S. 104, 112, "pricked out by the gradual approach and contact of decisions on the opposing sides." But an analysis of the decisions cited by the Attorney General will indicate that they fall in certain well-defined classes and that they are as we have already pointed out, governed by principles substantially different from those which are invoked to sustain this law. They may be assembled under the following heads:

Those concerned with the statutes regulating dealings in stocks on a margin.

Otis vs. Parks, 187 U. S. 606;
Brodnax vs. Missouri, 219 U. S. 285;
Gatewood vs. North Carolina, 203 U. S. 531.

Or regulating the business of banking.

Noble State Bank vs. Haskell, 219 U. S. 104;
Abilene National Bank vs. Dooley, 220 U. S. 1;
Engel vs. O'Malley, 219 U. S. 128;
Schaake vs. Dolley, 85 Kansas 598.

Or regulating employment agencies.

Williams vs. Fears, 176 U. S. 270, 275;
People vs. Brazee, 183 Mich. 259;
Brazee vs. Michigan, 15 Advance Opinions, 561.

Or regulating sales of goods in bulk.

Kidd, Dater Company vs. Musselman Grocer Company, 217 U. S. 461;
Lemieux vs. Young, 211 U. S. 489.

Or regulating the sale of oleomargarine.

People vs. Freeman, 233 Ill. 373;
People vs. Rotter, 131 Mich. 250;
Boyle vs. Pennsylvania, 127 U. S. 678.

Or regulating the size of loaves of bread.

People vs. Wagner, 86 Michigan, 594.

On regulating the stopping of trains.

L. S. & M. S. Ry. Co. vs. Ohio, 173 U. S., 285.

Or fixing a license fee upon an occupation.

Banta vs. City of Chicago, 172 Ill., 204.

Or determining Employers' liability.

C. B. & Q. Ry. vs. McGuire, 219 U. S., 578.

Or regulating the use of trading stamps.

Rast vs. Van Deman & Lewis, 240 U. S., 242;
Tanner vs. Little, 243 U. S., 369;
Pitney vs. Washington, 240 U. S., 387.

Or regulating insurance companies.

German Alliance Insurance Co. vs. Kansas, 233 U. S., 389.

The cases of *Rast vs. Van Deman & Lewis,* 240 U. S. 342, and *Tauner vs. Little,* 240 U. S. 369, which may be thought at first to have pricked out a new boundary of the police power, in reality rest upon a familiar rule. The Court declares that the trading stamp scheme "may not be called in an exact sense a 'lottery,' may not be called 'gaming,' it may, however, be considered as having the seduction and evil of such."

Rast vs. Van Deman & Lewis Company, supra, at page 365.

II

Interstate Commerce.

THE STATE IN THE EXERCISE OF ITS POLICE POWER HAS NO RIGHT TO PROHIBIT INTERSTATE TRADE IN LEGITIMATE ARTICLES OF COMMERCE. STOCKS, BONDS AND SECURITIES, AS DEFINED BY THIS ACT, ARE LEGITIMATE ARTICLES OF COMMERCE. THE TRAFFIC IN THESE ARTICLES BETWEEN TWEEN CITIZENS OF THE SEVERAL STATES IS INTERSTATE COMMERCE. THIS LAW PROHIBITS, BURDENS AND REGULATES THIS TRAFFIC AND IS, THEREFORE, IN CONFLICT WITH THE CONSTITUTIONAL PROVISION.

Stocks and bonds are articles of commerce.

The word "commerce" is not defined in the Constitution of the United States and has been said not to have any juridical meaning, but it is "a term of the largest import." It includes traffic by the purchase, sale and exchange of commodities and the transportation of persons and property by land and water. *Calvert, Regulation of Commerce,* citing *Welton vs. Missouri,* 91 U. S., 275, and other cases.

The term "commerce" received its first definition in *Gibbons vs. Ogden,* 9 Wheaton, 1. It was there said that "commerce is undoubtedly traffic; but it is something more, it is intercourse."

Under these broad definitions it would appear certain that stocks, bonds and securities which seem to be the very

vehicles of all modern trade and business, must be articles of commerce within the meaning of the Constitution. Such is in our opinion the doctrine of this Court.

The earliest case discussing this question is that of *Nathan vs. Louisiana,* 8 Howard 73. This case dealt with a tax by Louisiana on the business of issuing foreign bills. The Court said:

> "A bill of exchange is neither an export nor an import. It is not transmitted through the ordinary channels of commerce, but through the mail. It is a note merely ordering the payment of money, which may be negotiated by indorsement, and the liability of the names that are on it depends upon certain acts to be done by the holder, when it becomes payable."

The tax in the Nathan case was levied on the business. In the Michigan Blue Sky law the restriction is not on the business of selling stocks and bonds as a business. It affects, it is true, the "dealer" engaged in the sale of securities as a business but the vital principle of the law is the regulation of the *issue* sale of the securities.

In the Nathan case it was a tax the validity of which was in question. Here the law does not merely tax. It prohibits. In that case the tax was not levied on a bill of exchange moving in interstate commerce. Here interstate commerce in certain securities is prohibited. There the article subjected to the restrictions of the law was a note "ordering the payment of money." Here it is a thing of determined value, a chattle bought and sold and moving everywhere in commerce and trade.

The Nathan case was followed by *Paul vs. Virginia,* 8 Wallace 168, where court discussed a State statute providing for a State license of an insurance company and

held that the issuing of a policy of insurance is not a transaction of commerce. Justice Field said:

> "Issuing a policy of insurance is not a transaction of commerce. The policies are simply contracts of indemnity against loss by fire, entered into between the corporations and the assured, for a consideration paid by the latter. These contracts are not articles of commerce in any proper meaning of the word. They are not subjects of trade and barter offered in the market as something having an existence and value independent of the parties to them. They are not commodities to be shipped or forwarded from one State to another, and then put up for sale. They are like other personal contracts between parties which are completed by their signature and the transfer of the consideration. Such contracts are not inter-state transactions, though the parties may be domiciled in different States. The policies do not take effect—are not executed contracts—until delivered by the agent in Virginia. They are, then, local transactions, and are governed by the local law. They do not constitute a part of the commerce between the States any more than a contract for the purchase and sale of goods in Virginia by a citizen of New York whilst in Virginia would constitute a portion of such commerce."

The relation of insurance to commerce was again before the court in *New York Life Insurance Company vs. Deer Lodge County*, 231 U. S. 495, and the court again held that a policy of insurance was not an instrument of commerce. After reviewing the cases, the Court said:

> "A policy of insurance, the cases declare, is a personal contract, a mere indemnity, for a consideration, against the happening of some contingent event * * *."

> "It is contended that the policies are subject to sale and transfer, may be used for collateral security and other commercial purposes. This may be, but this use of them is after their creation, a use by the insured, not by the insurer."

We submit that there is a clear distincton between the executory insurance contract and the executed, valuable, vendible commodiy, the stock or bond. We can see some similarity between the process of issuing the certificate of stock and delivering it to the subscribing stockholder and the issue and delivery of an insurance policy but the transfer and sale of the issued certificate, like the pledge of the insurance policy by the insured, is an entirely different transaction. It is commerce in a vendible and valuable property. In other words the bond or the certificate of stock represetns a present executed contract right, a commodity passing freely from hand to hand and carrying value. It is vendible and confers valuable rights on its holder. These characteristics are not possessed by the insurance contract which has not yet been delivered to the insured.

The question at bar was however conclusively dealt with in the *Lottery Cases*, 118 U. S. 321. There the Court carefully considers its earlier decisions and elaborately discusses the question of what is and what is not an article of interstate commerce, and as well the general question of the scope of the phrase, "commerce among the states." Judge Harlan points out that "commerce among the states embraces navigation, intercourse, communication, traffic, the transit of persons and the transmission of messages by telegraph."

The Lottery Cases dealt with the constitutionality of an act of Congress to suppress the lottery traffic. It was in-

sisted that the sending of lottery tickets in interstate commerce did not constitute or evidence any transaction belonging to interstate commerce. The Government argued that lottery tickets, "title to which passes by delivery and which, from time immemorial, have been subjects of barter and sale are articles of commerce." The court gives the broadest interpretation to the word "commerce." Upon the direct question as to whether the lottery tickets were subjects of commerce, the court said, p. 353:

> "It was said in argument that lottery tickets are not of any real or substantial value in themselves, and therefore are not subjects of commerce. If that were conceded to be the only legal test as to what are to be deemed subjects of the commerce that may be regulated by Congress, we cannot accept as accurate the broad statement that such tickets are of no value. Upon their face they showed that the lottery company offered a large capital prize, to be paid to the holder of the ticket winning the prize, at the drawing advertised to be held at Asuncion, Paraguay. Money was placed on deposit in different banks in the United States to be applied by the agents representing the lottery company to the prompt payment of prizes. These tickets were the subject of traffic; they could have been sold; and the holder was assured that the company would pay to him the amount of the prize drawn. That the holder might not have been able to enforce his claim in the courts of any country making the drawing of lotteries illegal, and forbidding the circulation of lottery tickets, did not change the fact that the tickets issued by the foreign company represented so much money payable to the person holding them and who might draw the prizes affixed to them. Even if a holder did not draw a prize, the tickets, before the

> drawing, had a money value in the market among those who chose to sell or buy lottery tickets. In short, a lottery ticket is a subject of traffic, and is so designated in the act of 1895, 28 Stat. 963."

The dissenting opinion in this case was written by the Chief Justice and in the discussion of the question whether or not lottery ticket is an article of commerce, he reduces the problem to the question of whether or not the lottery tickets create a present contractual relation and whether or not they are vendible. He insisted that a lottery ticket is contingent in its nature, as is an insurance policy, and that it is not vendible.

The doctrine of the dissenting opinion, therefore, when applied to stocks and securities, has no force, since both a share of stock and a bond represent a completed contract. It is not contingent. It gives a present right and is vendible. One of the reasons why the defendants seek to sustain this law is because such stock and bonds are vendible to a degree.

In *Hatch vs. Reardon*, 204 U. S., 152, an earnest argument was made by eminent counsel against the constitutionality of the New York tax on the transfer of stock, and it was urged that the tax was void, among other reasons, because it violated the commerce clause of the United States. The Court declined to pass upon this question, saying that the case did not indicate that the parties were engaged in interstate commerce. The Court, however, did make the significant remark that "the immediate object of sale was the certificate of stock present in New York. That document was more than evidence, it was a *constituent of title*. No doubt, in a more remote sense the object was the membership or share which the certificate conferred or made attainable." The Court, therefore, declined to consider the question of whether or not a sale of

stock made by a resident of one state to a resident of New York, the stock passing from the first state to the second, was a transaction of interstate commerce. It did seem to indicate by its comments upon the fact that the certificate of stock was a "constituent of title," that if there had been such a sale, it would have been within the protection of the commerce clause and the law would have been bad unless it could be justified as a tax measure.

The case of *Engel vs. O'Malley*, 219 U. S., 128, upheld the Private Banking Act of New York. It was urged that this act violated the commerce clause of the constitution, but the Court declined to discuss this proposition insisting that there was no transaction in interstate commerce shown by the record. It did not discuss the question as to whether or not, if money had been received by the private banker and forwarded out of the state, it would be interstate or foreign commerce. The court said:

> "The law * * * was passed for the purpose of regulating and safeguarding the business of receiving deposits, which precedes and is not to be confounded with the later transmission of money, altho leading to it."

Here, again, the transaction held not to be interstate commerce is not identical with that set up in the case at bar.

The bill here recites that there is interstate commerce in stocks and bonds in Michigan. The owners transmit them to the purchaser in Michigan through the mail or otherwise and payment is made to the owner in the foreign state of his residence.

If a lottery ticket, which confers only a possible right upon the owner to participate in a fund, is to be held an article of commerce, why should not a certificate of stock

be likewise an article of commerce? It represents an actual value. It creates a present property right and it is a constituent of title. It is dealt in. It is a subject of trade and barter. It is vendible. The distinction that it passes through the mail, as was suggested in the Nathan case, is of no value, since all classes of property now pass through the mails. Certificates of stocks and bonds travel by express, as well as by mail. In many instances, their title passes by delivery, as does the title to other personal property.

Bills of lading have been held to be article of commerce. *Almy vs. State of California*, 24 Howard 169. How much more should a bond be an article of commerce when the sale thereof can be consummated by delivery and when it is, according to modern commercial usage, handled, taxed and treated as a thing of value.

We respectfully submit that to hold that the stocks and securities of the character described in the Michigan Act are not articles of commerce runs counter not only to the law, but as well to the theory of modern business and to all the practices of modern finance.

(b) *The State in its police power cannot burden interstate commerce in legitimate articles of such commerce. Stocks and bonds are such legitimate articles.*

The language of the Court in *Simpson vs. Shepard*, 230 U. S. 352, is pertinent here.

After explaining that the power of Congress to regulate commerce of the several states is supreme and plenary, "it is complete in itself, may be exercised to its utmost extent and acknowledges no other limitations than are prescribed by the constitution," the opinion proceeds to set forth "what the states cannot do."

> "The states are not permitted directly to regulate or restrain that which by its nature should be under the control of the one authority and be free from restriction save as it is governed in the manner that the national legislature constitutionally ordains. * * * They have no power to prohibit interstate trade in *legitimate articles of commerce.*"

There can be no doubt but that stocks, bonds and securities are legitimate articles of commerce. In our view, the words "legitimate articles of commerce" mean no more than if the court had said, "Lawful articles of commerce" or, indeed, "articles which belong to commerce," or, again, "commercial articles"; "undoubted articles."

In the case of *Bowman vs. Chicago etc. Ry Co.*, 125 U. S. 465, 489, the Court had the following to say, quoting from the opinion of Justice Catron in the *License Cases*, 5 Howard 504, 599:

> "The assumption is, that the police power was not touched by the Constitution, but left to the States, as the Constitution found it. This is admitted; and whenever a thing, from character or condition, is of a description to be regulated by that power in the State, then the regulation may be made by the State, and Congress cannot interfere. But this must always depend on facts subject to legal ascertainment, so that the injured may have redress. And the fact must find its support in this, whether the prohibited article belongs to, and is subject to be regulated as part of foreign commerce, or of commerce among States. If, from its nature, it does not belong to commerce, or if its condition, from putrescence, or other cause, is such, when it is about to enter the State, that it no longer belongs to commerce, or, in other words, is not a commer-

cial article, then the State power may exclude its introduction. And as an incident to this power, a State may use means to ascertain the fact. And here is the limit between the sovereign power of the State and federal power. That is to say, that which does not belong to commerce is within the jurisdiction of the police power of the State; and that which does belong to commerce is within the jurisdiction of the United State. And to this limit must all the general views come, as I suppose, that were suggested in the reasoning of this Court in the cases of *Gibbons vs. Ogden, Brown vs. The State of Maryland*, and *New York vs. Miln.*"

Again in the same case, quoting from *Railroad Co. vs. Husen*, 95 U. S. 465, 472, the Court said:

"While we unhesitatingly admit that a State may pass sanitary laws, and laws for the protection of life, liberty, health, or property within its borders; while it may prevent persons and animals suffering under contagious or infectious diseases, or convicts, etc., from entering the State; while for the purpose of self-protection it may establish quarantine, and reasonable inspection laws, it may not interfere with transportation into or through the State, beyond what is absolutely necessary for its self-protection. It may not, under the cover of exerting its police powers, substantially prohibit or burden either foreign or interstate commerce. * * *

The reach of the statute was far beyond its professed object, and far into the realm which is within the exclusive jurisdiction of Congress. * * * The police power of a State cannot obstruct foreign commerce or interstate commerce beyond the necessity for its exercise; and, under color of it, objects

> not within its scope, cannot be secured at the expense of the protection afforded by the Federal Constitution. And as its range is sometimes very near to the field committed by the Constitution to Congress, it is the duty of the Courts to guard vigilantly against any needless intrusion."

So in *Crutcher vs. Kentucky,* 141 U. S. 47, 60, 61, the power of the state over "deleterious or injurious" articles was recognized but it was said that "it is only such things as are clearly injurious to the lives and health of the people that are placed beyond the protection of the commercial power of Congress."

But the Blue Sky Law in question in this case can neither be classified as a sanitary measure or a quarantine law. It is not an inspection law as we have already pointed out.

Does the possibility of fraud in the sale of the security compel a different conclusion? It must be remembered that the fraud cannot be consummated until the sale is completed. It is not inherent in the certificate of stock itself. It is the composite result of the representation of the seller, the character of the security sold, the price, and the knowledge of the buyer. The "inspection" therefore of the article of commerce can give no indication as to the evil the statute is said to be intended to prevent.

For this reason the statute provides, not for an inspection of the article transmitted in interstate trade, but for an examination of the property as to which the security is given, prior to the negotiation of that security. This examination values that property and in actuality fixes the price upon the security. "Inspection" is not a proper word to apply to this process. But whatever it may be called it recognizes that the article of commerce with which it deals, that is the bond or stock, is entirely different apart from the "deleter-

ious" articles of commerce subject to State regulation and inspection.

The Provisions of the Act Constitute a Substantial Burden on Interstate Commerce and the Act is Therefore Void.

But even if the law be sustainable as within the police power, still it does so *directly* burden interstate commerce as to be invalid for that reason, that is, invalid so far as interstate commerce is concerned. In other words, to paraphrase the language of the opinion of the lower Court there may be a field for the exercise of the police power legitimate from all other points of view and yet forbidden as against interstate commerce and this law lies within that field.

Says Prof. Willoughby in his work on the Constitution, p. 664:

> "In the exercise of these powers it is often the case that interstate and foreign commerce are indirectly and even substantially affected. But in no case can regulation of interstate and foreign commerce be the direct or primary aim of the State's action. If this is the aim or effect, no support for the validity of the law may be obtained by calling the law a police regulation."

Yet the direct and primary aim of this statute is the regulation of interstate commerce. It is insisted by the State that the law is intended "to stop the sale of stock in fly-by-night concerns, visionary oil wells, distant gold mines and other fraudulent organizations." The State of Michigan guards its own corporate organization with the greatest care. Under its statutes only tangible values can be capitalized. It is not its local corporations or its local stocks and securities which are the real object of this law's solicitude. It is rather the dealings in Michigan in the

foreign securities at which the law strikes. Such dealings can hardly be separated from interstate commerce.

But even if it be not directed at interstate commerce, it still may substantially prohibit or burden that commerce. As we have said, if the statute has no justification in the police power it is surely not only a burden on interstate commerce but an unjustifiable burden as well, and even if it is within the police power of the state it may be still a direct restraint on interstate business.

Let us again inquire as to its restrictions.

The law absolutely prohibits the issue and sale of all stocks, bonds and securities as there defined for a period limited only by the will of the Commission. Can it be said that this restriction is, to use the language of *Railroad vs. Husen, supra* within "the necessity for its exercise," that is the exercise of the police power? Can the Court say that fraud is so prevalent in the sales of securities or the borrowing of money on bonds and mortgage and secured paper, that an admittedly honest transaction can be for one hour suspended and for that purpose the domain of the federal government can be thus invaded?

But there are other direct and substantial burdens on interstate trade. A "license" fee is to be exacted on every security offered.

The cases of *Crenshaw vs. Arkansas*, 227 U. S. 389, *Rogers vs. Arkansas*, 227 U. S. 409, and *Adams Express Co. vs. City of New York*, 232 U. S. 14, dealt with a state requirement for a license to conduct interstate business. They are now directly in point because this law prohibits a dealer doing business with a *license* (See Section 11).

In the *Crenshaw* case the Court declared a license law void at the suit of one who did an interstate business.

In *Adams Express Co. vs. New York,* 232 U. S. 14, the Court dealt with an ordinance requiring a license of express drivers. The opinion says:

> "Undoubtedly, the exertion of the power essential to assure needed protection to the community may extend incidentally to the operations of a carrier in its interstate business, provided it does not subject that business to unreasonable demands and is not opposed to Federal legislation. *Smith vs. Alabama,* 124 U. S. 465; *Hennington vs. Georgia,* 163 U. S. 299; *N. Y., N. H. & H. R. R. Co. vs. New York,* 165 U. S. 628; *Lake Shore & M. S. Ry. Co. vs. Ohio,* 173 U. S. 285. It must, however, be confined to matters which are appropriately of local concern. It must proceed upon the recognition of the right secured by the Federal Constitution. Local police regulations cannot go so far as to deny the right to engage in interstate commerce, or to treat it as a local privilege and prohibit its exercise in the absence of a local license. *Crutcher vs. Kentucky,* 141 U. S. 47, 58; *Robbins vs. Shelby County Taxing District,* 120 U. S. 489, 496; *Leloup vs. Mobile,* 127 U. S. 640, 645; *Stoutenburgh vs. Hennick,* 129 U. S. 141, 148; *Rearick vs. Pennsylvania,* 203 U. S. 507; *International Text Book Co. vs. Pigg,* 217 U. S. 91, 109; *Oklahoma vs. Kansas Natural Gas Co.,* 221 U. S. 229, 260; *Buck Stove Co. vs. Vickers,* 226 U. S. 205, 216; *Crenshaw vs. Arkansas,* 227 U. S. 389; *Minnesota Rate Cases,* 230 U. S. 352, 401. As was said by this Court in *Crutcher vs. Kentucky,* 141 U. S. p. 58, 'a state law is unconstitutional and void which requires a party *to take out a license for carrying on interstate commerce, no matter how specious the pretext may be for imposing it?*'"

The requirement that the foreign investment company and the foreign dealer must appoint an agent for service of process is likewise a direct and substantial burden.

In the case of *Sioux Remedy Co. vs. Cope*, 235 U. S. 197, the State of South Dakota required the foreign corporation to subject itself to jurisdiction in all the courts of the state before it could sue to enforce a contract arising out of interstate commerce. In the Blue Sky law a foreign corporation must subject itself to the jurisdiction of the state courts before it can make a delivery of securities in interstate commerce. The South Dakota statute was defended as within the police power of the state. The State Court held it to be a reasonable exercise of the police power. The United States Supreme Court denied this.

> "It may be conceded in a general way that a State may restrict the right of a foreign corporation to sue in its courts. *Bank of Augusta vs. Earle*, 13 Pet. 519, 589-591; *Anglo American Provision Co. vs. Davis Provision Co.*, 191 U. S. 373. And in the same general way it may be conceded that a State may restrict the right of such corporations to engage in business within its limits. *Paul vs. Virginia*, 8 Wall. 168; *Hooper vs. California*, 155 U. S. 648. But the power so to deal with these subjects, like all other state powers, can only be exerted within the limitations which the Constitution of the United States places upon state action. *Missouri vs. Lewis*, 101 U. S. 22, 30; *Blake vs. McClung*, 172 U. S. 239, 256; *Chambers vs. Baltimore & Ohio R. R. Co.*, 207 U. S. 142, 148; *Western Union Telegraph Co. vs. Kansas*, 216 U. S. 1,, 33; *Southern Railway Co. vs. Greene*, 216 U. S. 400, 413. One of these limitations is that before indicated arising from the commerce clause, whose operation, as this

Court has said, is such that a corporation authorized by the State of its creation to engage in interstate commerce 'may not be prevented by another State from coming into its limits for all the legitimate purposes of such commerce.' *Western Union Telegraph Co. vs. Kansas*, 216 U. S. 1, 27. We think that when a corporation goes into a State other than that of its origin to collect, according to the usual or prevailing methods, the purchase price of merchandise which it has lawfully sold therein in interstate commerce, it is there for a legitimate purpose of such commerce, and that the State cannot, consistently with the limitation arising from the commerce clause, obstruct or hamper the attainment of that purpose. If it were otherwise, the purpose of the Constitution to secure and maintain the freedom of commerce by whomsoever conducted could be largely thwarted by the States and the commerce itself seriously crippled."

We conclude therefore that the Act is a direct burden on interstate commerce and also that if it is not such a direct burden it is yet so burdensome and so unreasonably restrictive that it is in conflict with the Commerce Clause of the Constitution and therefore void.

III

The Statute Is Void Since It Vests Arbitrary Power in the Commission.

The third main objection to the Act relates to the arbitrary power granted the Commission. It is a reiteration of the general objection that the Act is unreasonable in its restrictions and so beyond the police power, but it goes beyond that. It inquires whether the state can set up a Commission vested with executive, legislative and judicial authority which can arbitrarily determine the right to do the acts there described. The *opinion* of the Commission that the sale of the securities will work a fraud is the standard for the determination of the right of a citizen to issue and sell securities. We refer to the action of the Commission as arbitrary because it is not based on a finding that fraud exists. It is an *opinion* of a possibility or probability of future fraud. "Broader or vaguer language could not be chosen. It subjects to the practically uncontrolled discretion of the Commission every issue or general sale of stocks, bonds or securities hereafter to made in Michigan." *Alabama Transp. Co. vs. Doyle et al* 210 Fed. 173.

That there must be primary standard in the law for the action of the Commission is settled by many cases.

The rule was laid down in the case of *Yick Wo vs. Hopkins, Sheriff*, 118 U. S. 356, where an ordinance was held void which made it unlawful for any person to maintain a laundry in a frame building in San Francisco without first obtaining a permit from the board of supervisors. The opinion is in part as follows (p. 366):

"There is nothing in the ordinances which points to such a regulation of the business of keeping and conducting laundries. They seem intended to confer, and actually do confer, not a discretion to be exercised upon a consideration of the circumstances of each case, but a naked and arbitrary power to give or withhold consent, not only as to places, but as to persons. So that, if an applicant for such consent, being in every way a competent and qualified person, and having complied with every reasonable condition demanded by any public interest, should, failing to obtain the requisite consent of the supervisors to the prosecution of his business, apply for redress by the judicial process of *mandamus*, to require the supervisors to consider and act upon his case, it would be a sufficient answer for them to say that the law had conferred upon them authority to withhold their assent, without reason and without responsibility. *The power given to them is not confided to their discretion in the legal sense of that term, but is granted to their mere will. It is purely arbitrary, and acknowledges neither guidance nor restraint.*"

This doctrine has been repeatedly confirmed. We do not intend to cite all the cases dealing with it, but certain of them deserve attention.

In *United States vs. Grimaud*, 220 U. S. 506, the Secretary of Agriculture had made a rule requiring permits for grazing stock on a public reserve. It was objected that this was a delegation of legislative power. But the court declared that the general rule had been laid down in the statute. The object of the reservation was stated in the law, and the secretary had authority to supplement it by appropriate special regulations.

In *Red "C" Oil Mfg. Co. vs. Board of Agriculture*, 222 U. S. 380, the legislature required that illuminating oils be

safe, pure and afford a satisfactory light. It was left to the Board of Agriculture to determine what oils would measure up to these standards. The Court said, "We think a sufficiently primary standard was established and that the claim that legislative powers were delegated is untenable."

But where is the primary standard here? What general rule is there laid down in this statute? Its language is:

> "If said Commission finds that the proposed plan of business of said investment company, or that its proposed contracts, stocks, bonds or other securities are fraudulent or are of such a nature that the sale of such contracts, stocks, bonds or other securities *would in the opinion* of said Commission work a fraud upon the purchaser, etc."

Aside from the finding that the securities are fraudulent, the test is *the opinion* of the Commission that the securities *will* work a fraud.

It is the *opinion*, not the fact, that is the basis of the ruling. It is the *probability*, not the actual presence of fraud, which is here the test. Surely here is no "primary standard," but a clear delegation of arbitrary authority. For if the Commission declares that in its opinion fraud will result, where is the relief? It cannot be objected that fraud will not result, because it is the *opinion* which is the final test. And as to the probability, there can be no proof, only an opinion.

In *Schaezlein vs. Cabaniss*, 135 Cal. 466, the statute gave the labor commissioner power to direct the installation of a mechanical contrivance in factories where "dust, filaments or injurious gases are generated or produced that are *liable* to be inhaled by the persons employed therein." The Court condemned the statute, saying in part:

> "Nor does it matter if the condition of such a workshop be reasonably wholesome for the use of

> the operatives, if 'dust, filaments, or injurious gases' are 'liable to be inhaled' (and *it is here the liability, and not the fact, of the inhalation which invites the action* of the Commission), and if, *in the opinion of the commissioner, such liability* to inhalation could 'to a great extent' be prevented, he may designate and prescribe the kind of appliance which in his judgment is suitable for such purpose, and it must be employed."

It is pertinent here to refer to the exemption of the so-called "Manual" securities.

The law provides that any security listed in a "so-called Manual of Information" is exempted from the operation of the statute. The theory is that this listing in a "Manual" certifies that the investment company is not fraudulent and that the sale of its security will not work a fraud. There is no question but that these Manuals do not pretend to certify even the solvency of the concerns advertising in their pages. Much less do they pretend to say whether or not the securities there listed may not be sold under circumstances which will work a fraud on the purchaser.

The wholesale approval of the Manual is therefore a delegation by the Legislature, not to the Commission, but to the publisher of the Manual, of the arbitrary power to permit the sale of the security in Michigan. There is here no finding of any kind whatever nor any action by the Commission. The purchase of advertising space will give the stocks and bonds the same standing and approval as the formal finding and approval of the Commission.

In discussing this question of delegation of arbitrary power, we make no question of the right of the Legislature to delegate certain powers to an administratrive commission. But we insist that there must be a "primary stand-

ard" for the Commission's action. The probability that some evil will arise in the future is not such a standard.

We have carefully read the brief for the appellants but we find in it no reference to the undoubted fact that the final test of the law in question lies in the opinion of the Commission that fraud will probably result from the sale of the securities. Frequent reference is made to the finding of the Commission that fraud exists, and as to whether "the issue is fraudulent or not." We do not quarrel with the proposition that a delegation of the Commission to determine actually existing fraud would set up a sufficient standard in the law so that it could be defended against the objections that an arbitrary power had been conferred. But it is with the delegation to the Commission and to the publisher of the Manual of the power to determine according to its opinion that fraud will probably result, that we disagree. It is this attempt to confer arbitrary power which the learned Attorney General does not refer to nor attempt to sustain.

IV.

The Title To the Act Covers More Than One Object and Does Not Express the Objects Set Forth In the Statute.

Section 21, Art. 5 Constitution of Michigan:

> "No law shall embrace more than one object, which shall be expressed in its title."

The title to the Blue Sky Act defines the purpose of the Act as the prevention of "fraud in the sale and disposition of stocks" etc., by requiring an inspection etc., and regulation and supervision, etc.

Its language, however, is confusing. It will be noted that it is "to prevent fraud in the sale of securities by any dealer, firm, company, association," etc., by requiring an inspection etc. and such regulation and supervision of the business of *said persons, firms*, etc. *Persons* must refer to *dealers* who sell securities. The language does not indicate an intent to regulate *persons* who *issue* securities. In fact it is difficult to read into the title any reference except to dealers. The use of the words *"including dealers and agents"* is the only thing to indicate a broader scope than the regulation of dealing in securities. And the body of this Act clearly covers *persons* who issue securities since it covers all those who issue as well as those who deal in the securities there defined.

There are in it, however, other provisions which do not square with this title.

Is the provision authorizing the Commission to appraise the investment company's property within the meaning of

the words of the title? The title covers "inspection" and "supervision." The power, however, to compel the surrender of stock already issued and the consequent amendment of the company charter, if that power exists, surely is not described in a title which indicates only supervisory powers.

Would one reading the title to the Act suppose that it prohibited the sale of securities which are not fraudulent but which had been issued in payment of property taken at a price which was in the opinion of the Commission beyond its real value?

Would any one suppose that it gave the Commission authority to prevent the sale of stock by one holder unless a proportion of the stock of the other holders thereof was given up and cancelled, even though such other holders did not desire to sell stock in Michigan?

There is nothing in the title to indicate that a newspaper is to be punished in a criminal action if it publishes certain advertisements.

The Act requires that all the books of accounts of the investment company shall be open to "stockholders and investors in said Company." Where is the suggestion in the title that the law contains this enlargement of the rights of stockholders and investors, whoever the word investors may be taken to include?

The title to the Act refers to the repeal of the 1913 statute. The Act itself repeals this law but preserves the proceedings pending hereunder. Does the title indicate this sufficiently?

The title says nothing as to the creation of a Commission to administer the law. Does the reference to inspec-

tion and regulation sufficiently include and sufficiently indicate the creation of such a Commission?

We do not think it can be said of this Act that "the broad language of the title is capable of a construction which will cover all the provisions of the Act." *Alabama Transp. Co. vs. Doyle*, 210 Fed. 173.

V.

The Statute is Class Legislation and is Therefore Void.

The principle which controls the question of class legislation is well known. It was succinctly stated in *Richie vs. Wayman,* 241 Ill. 549, as follows:

> "A law which is made applicable to only one class of citizens, however, must be based upon some substantial difference between the situation of that class and other individuals to which it does not apply."

With this rule in mind, let us examine the statute under discussion. Are the business enterprises exempted from the operation of this act any different in character, so far as the purpose of this act is concerned, than those to which the act applies? Are the securities exempted from the operation of this act any different, so far as the purpose of this act is concerned, from those to which the Act applies?

The 1913 Act was criticized because of the evident discrimination between individuals and partnerships and between long and short time paper, between ordinary mortgages and trust mortgages, etc.

Some attempt has been made to correct these defects. The 1915 law now refers (Section 2) to the individual person. But other discriminations have appeared.

In the effort to eliminate the objection made as to the inclusion of long time commercial paper in the 1913, "*unsecured commercial paper*" has been exempted. This

makes a still greater discrimination. It immeasurably broadens the scope of the Act and makes it interfere with ordinary commercial business far more than did the 1913 Act. What is "secured commercial paper" or "unsecured commercial paper"? Secured commercial paper in the ordinary commercial phrase includes paper secured by the deposit of collateral and papers secured by endorsement. Practically all commercial paper taken by banks is secured and so within the language of the Act. There is a class of commercial paper sold by brokers to banks—paper of large mercantile and manufacturing concerns—which may not be endorsed or secured in any way, and this, by the way, would come the nearest to that which the Commission might wish to regulate. But the ordinary paper handled by the banks, the vast volume of acceptances and trade notes given by mercantile and manufacturing houses, this all comes to the bank and the money lender with security either by way of collateral or endorsement. Why should this be covered by the Act and the unsecured paper be not covered? If any paper needs regulation it would seem that which has no security.

This anomaly of the law is of sufficient importance to justify the condemnation of the court.

The Act excludes securities of "any domestic *corporation organized without capital stock and not for pecuniary gain or* exclusively for educational, benevolent, charitable or reformatory purposes."

With this exemption in the Act a corporation so organized may issue bonds and sell them without compliance with the law. Granted that the proposed regulation is necessary, what is the distinction, so far as the purchaser of the security is concerned, between the corporation organized for profit and that organized not for profit? The test under the law, at least so reads the title, is the fraud

in the *security*. How is the purpose of the corporation of any assistance in determining that question?

The law exempts *mortgages* on property within this State when the entire debt is sold with the mortgage. But where the mortgage is on the property without the State the law applies even though the whole debt is sold with the security.

The law exempts securities listed in *"Standard Manuals of information."*

Yet these so-called "Manuals" do not attempt to furnish the information required by the Commission of the investment companies. They, of course, connot deal with the representations made by any one who attempts to sell any security listed therein. The exemption, therefore, of securities listed in the "*Manuals*" is a gross discrimination against securities not so listed. It amounts to a suggestion that advertising space be purchased in these directories. A corporation unwilling to pay the "Manual" fee is subject to the inconveniences of the Act and may be prevented from selling its securities though, if it subscribes to the "Manual," it has the open sesame to do business in Michigan.

The Act forbids *"taking subscriptions for"* stock unless there is compliance with its terms. But it exempts *stock dividends*. Very evidently the character of a stock dividend was misunderstood. A stock dividend is effected by the declaration of a property dividend. The stockholders then waive their right to the property and consent to take stock. The transaction in its essentials is equivalent to a stock subscription to be paid in property. There can be no justification in drawing a distinction between them.

VI.

The Act Delegates to the Michigan Securities Commission Legislative Authority. It is Therefore Contrary to the Provisions of the Constitution.

We have already discussed this subject insofar as it deals with the arbitrary power given to the Commission.. But apart from the question of whether or not this arbitrary power in the Commission is unreasonably destructive of private rights there is, of course, the problem of whether or not legislative power has been delegated to the Commission. Insofar as we can separate this phase of the problem we desire now to invite to it the Court's attention.

The functions of the Securities Commission are various. They combine the administrative, judicial and the legislative. It is an administrative board in its examination of investment companies. It is a judicial body insofar as it finds whether or not the proposed plan of business of the Investment Company is fraudulent or whether its securities are fraudulent or of such a nature that their sale would, in the opinion of the Commission, work a fraud.

Is there any standard set up in the law by which this finding of the Commission can be measured? Without it the Commission must itself exercise legislative power. That such a standard is necessary is settled by the decisions we have already examined. "The power conferred on the legislature to make laws," says Cooley, 7th Ed. 163, "cannot be delegated by that department to any other body or authority." See also the following cases:

Yick Wo vs. Hopkins, Sheriff, 118 U. S. 356;

U. S. vs. Grimaud, 220 U. S. 506;

Schaezlein vs. Cabaniss, 135 Cal. 466;
Red "C" Oil Mfg. Co. vs. Board of Agriculture, 222 U. S. 380.

In *Dowling vs. Insurance Co.*, 92 Wis. 63, in dealing with a statute which intrusted to the Insurance Commissioner the power of framing the standard insurance policy, the Court said:

> "The result of all the cases on this subject is that a law must be complete, in all its terms and provisions, when it leaves the legislative branch of the government, and nothing must be left to the judgment of the electors or other appointee or delegate of the legislature, so that, in form and substance, it is a law, in all its details, *in praesenti*, but which may be left to take effect *in futuro*, if necessary, upon the ascertainment of any prescribed fact or event."

In *State vs. Burdge*, 95 Wis. 397, the Court had before it the rule of a board of health excluding from the public schools children who had not been vaccinated. No statute had been passed compelling vaccination. The Court said:

> "The making of such rules and regulations is an administrative function, and not a legislative power, but there must first be some substantive provision of law to be administered and carried into effect. The true test and distinction whether a power is strictly legislative, or whether it is administrative, and merely relates to the execution of the statute law, 'is between the delegation of power to make the law, which necessarily involves a discretion as to what it shall be, and conferring authority or discretion as to its execution, to be exercised under and

in pursuance of the law.' The first cannot be done. To the latter, no valid objection can be made."

In statutes dealing with the delegation of powers to boards to issue licenses, a standard of proficiency has been set, else the law has been held bad.

In *Harmon vs. State*, 66 Ohio St. 249, the language of the statute was:

> "If, upon examination, the applicant is found trustworthy and competent."

It was said that each examiner might "have his own notions as to what shall contitute an applicant 'trustworthy and competent.' "

A Kentucky statute authorized a state board to revoke the license of a physician for "grossly unprofessional conduct of a character likely to deceive or defraud the public." This act was held bad because no standard had been prescribed to determine whether such conduct was or was not unprofessional.

> *Mathews vs. Murphy*, Ky. Court of Appeals, 63 S. W. 785.

In the opinion of the lower Court on the 1913 Statute, it was said:

> "Of like effect and subject to like infirmity is the provision forbidding the sale of securities, if the Commission thinks the Company's organization or proposed plan of business is not 'fair.' Broader and vaguer language could not be chosen. It subjects to the practically uncontrolled discretion of the Commission every issue or general sale of stocks, bonds or securities hereafter to be made in Michigan."

This language applies as aptly to the provision in the present law forbidding the sale of securities which in the *opinion* of the Commission will work a fraud. There might be said to be an indefinite standard in the word "fair," but when the *opinion* of the Commission is substituted for a finding as to existing facts there is surely a delegation of the Legislative authority and power.

VII.

The Statute Attempts to Confer Upon the Michigan Securities Commission Judicial Powers. It is, Therefore, in Violation of the State of Michigan.

But whether a standard has been set by the legislature or is to be fixed by the Commission, the application of the statute and that standard to any particular state of facts calls for a judicial determination. There must be a judicial determination of whether or not a given investment company or a given security is fraudulent or whether or not the sale of the security will in the opinion of the Commission work a fraud.

Under the statute the Michigan Securities Commission must determine, as a Court, what are the facts in connection with the plan of business, the articles of association and by-laws of a corporation and find whether the same are fraudulent or will work fraud. There is, therefore, an admitted creation of judicial authority in the Commission.

In the case of *Chandler vs. Nash*, 5 Mich. 409, Judge Christiancy had under consideraton a statue which gave a notary public power to hear and determine questions both of law and of fact. He laid down the rule that so long as the constitution vested the whole judicial power in the Courts and officers named in that instrument, it could not be conferred upon any others.

In *Andrews vs. Judge of Probate*, 74 Mich. 278, the Court had under consideration an act which provided for the naming of a board of examiners of elections. The Court said:

> "If it (the act) confers judicial powers on the Board of Examiners, to that extent it is invalid. The Constitution vests the judicial power in certain specified Courts, and it cannot be legally vested elsewhere. If this act confers upon the Board of Examiners authority to investigate and adjudicate upon any fraud in the election, it cannot be sustained in that respect."

If there was any doubt hat it was intended by the statute that this Commission should be a judicial body clothed with power to judicially determine as to the specific matters above set forth, it is removed by the provisions of Section 22, which provides a review of the findings and orders of the Commission upon a writ of certiorari direct to the Supreme Court of the State.

> "Certiorari does not lie to review acts which are *not done in the exercise of judicial power* or authority but are merely ministerial, executive or legislative in their character."
>
> *Root vs. Barnes*, 1 Mich. 37;
>
> *6 Cyc. of Law and Procedure*, 753.

VIII.

CONCLUSION.

The Law Cannot Accomplish Its Purpose and Finds No Justification in General Business Conditions Nor in the Fact That Similar Statutes Have Been Passed in Other States.

Of what real efficacy can a law be which rests its test or standard on probabilities and the unregulated opinion of an administrative commission. This commission assumes to examine and regulate every form of business, every kind of security, barring only those specifically excepted by the Act. It assumes to probe the intentions of the issuers and sellers of these securities and to determine whether they will in the future deceive the purchasers. Manifestly one can falsify as to the value of a valuable security as well as that of a valueless one. It proposes to determine how far the purchasers even of a doubtful security will be defrauded. Even if the doubtful security may be thereafter bought on an honest statement by a wary and fully informed buyer, still if the Commission's opinion is that fraud will arise an honest sale is forbidden.

And it is physically impossible for the Commission to examine all the securities issued and offered for sale. Omniscience alone would enable it to do its full legal duty. Only by a resort to the provision as to the Manuals can any progress be made. For the act would, of course, be entirely impossible of execution if it were not for this provision exempting securities listed in the so-called "Manuals." All the great mass of securities already issued are at once approved without information to or examination by the

Commission. An advertisement becomes as efficacious as a comprehensive report to the Commission and an investigation and appraisal of the applicant's property.

These objections, however, go mainly to the provisions of the law and not to its basic principle. That rests as we have already urged upon a false conception of business dealings and commercial practises. They are not generally or essentially fraudulent.

Nor does the fact that in many states, led on by the catch-word "Blue Sky," hysterical legislatures have attempted to write these laws upon the statute books. They may or may not be open to the same objections as this one in Michigan. It is, however, interesting to note that wherever a similar statute has been presented to the Courts it has been condemned. Those which have been sustained differ radically and essentially from the Michigan law.

Wm. R. Compton Co. vs. Allen, 216 Fed. 537;
Bracey vs. Darst, 218 Fed. 482;
Ex parte Taylor, 68 Fla. 61;
Standard Home Co. vs. Davis, 217 Fed. 904.
Geiger-Jones Co. vs. Turner, 230 Fed. 233.

We respectfully submit that the law is unconstitutional and should be so held.

HAL H. SMITH,
Attorney for Appellants, Weis Fibre Container Corporation, et al.